Supreme Court, U.S.
FILED
95-44 JUL 7 - 1995
No. OFFICE OF THE CLERK

In The

Supreme Court of the United States

October Term, 1995

RICHARD C. BECHERER, *et al.*,

Cross-Petitioners,

v.

J. DON ADAMS, MERRILL LYNCH, PIERCE, FENNER & SMITH, *et al.*,

Cross-Respondents.

On Petition For A Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

CROSS-PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

1. Whether section 28(a) of the Securities Exchange Act of 1934, which limits a plaintiff to *recovery* of judgments in an amount not in excess of the plaintiff's actual damages, prohibits a plaintiff who has been *granted* a judgment against one defendant, from seeking to *obtain* judgments against other defendants who also may be liable for the plaintiff's injuries.

2. Whether the United States Court of Appeals for the Sixth Circuit (the "Court of Appeals") deprived Petitioners of valuable property rights without due process of law, as guaranteed by the Fifth Amendment to the Constitution, by ruling that, since Petitioners had obtained a judgment on a contract claim against one (admittedly insolvent) defendant, Petitioners were barred from proceeding with cognizable tort claims arising out of the same transaction against other potentially joint and severally liable parties because, in the Court of Appeals' view, allowing Petitioners to proceed with their tort claims (regardless of the merits) would result a "double recovery" or "windfall" to Petitioners, in violation of Section 28(a) of the Securities Exchange Act of 1934.

LIST OF PARTIES

The parties to the proceeding in the United States Court of Appeals for the Sixth Circuit were (1) Richard C. Becherer; Lawrence Milton Richard; Robert A. Horvath; Shirley L. Horvath; Henry V. Denolf; and Joann L. Denolf, on behalf of themselves and a certified class of all others similarly situated, Plaintiffs-Appellants and Cross-Appellees; (2) J. Don Adams, *et al.*, Proposed Intervenors, Appellants and Cross-Appellees; (3) Merrill Lynch, Pierce, Fenner & Smith, Inc.; Frank Lavin; Martin Cicco; Laventhol & Horvath; M.A. Mortenson Company; Winsor/Faricy Architects, Inc.; Trustbank Mortgage Center, Incorporated; and Midwest Title Guarantee Company of Florida; Appellees; and (4) Can-American Corporation; Can-American Realty Corporation; Shelter Seagate Corporation; Garrett G. Carlson; Graham C. Lount; and Arni Thorsteinson, Appellees and Cross-Appellants.

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OPINIONS BELOW

The opinion of the Court of Appeals is reported at 43 F.3d 1054, and is reprinted at App. 1a of the Petition for Writ of Certiorari filed by J. Don Adams, *et al.*, Case No. 94-1968 (the "Adams Petition"). The November 19, 1990 opinion of the United States District Court for the Eastern District of Michigan (the "District Court") is unreported and is reprinted at App. 1 of the Appendix hereto. The August 7, 1992 opinion of the District Court is reported at 799 F. Supp. 755 and is reprinted at App. 11 of the Appendix hereto. The November 24, 1992 opinion of the District Court is reported at 809 F. Supp. 1259 and is reprinted at App. 1b of the Adams Petition.

JURISDICTION

The Court of Appeals entered its judgment on January 10, 1995. The Court of Appeals entered its order denying Petitioners' Motion for Rehearing and/or Rehearing *in banc* on April 11, 1995. (Adams' Petition, at App. 1d.) The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Section 28(a) Of The Securities Exchange Act Of 1934, 15 U.S.C. § 78bb(a) (in relevant part):

The rights and remedies provided by this title shall be in addition to any and all other rights and remedies

that may exist at law or in equity; but no person permitted to maintain a suit for damages under the provisions of this title shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the act complained of. . . .

Fifth Amendment To The U.S. Constitution:

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

STATEMENT OF THE CASE

A. Introduction

This Cross-Petition presents the issue of whether Petitioners, who have obtained a judgment against one defendant (who is admittedly uncollectible), can be precluded from prosecuting other cognizable claims arising out of the same transaction against other potentially joint and severally liable defendants solely on the ground that, if allowed to do so, Petitioners might improperly obtain a "double recovery" or "windfall", in violation of section

28 of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb(a), and the common law. Petitioners submit that such a holding by the Court of Appeals not only conflicts with the decisions of this Court and every other United States court of appeals that has considered the issue, but also so departs from the accepted and usual course of judicial proceedings as to deprive Petitioners of valuable property rights (choses in action), in violation of Petitioners' fundamental rights to due process of law under the Fifth Amendment to the Constitution. Accordingly, Petitioners request that their Cross-Petition for Writ of Certiorari be granted and that the decision of the Court of Appeals be summarily reversed pursuant to Supreme Court Rule 16.1.

B. Summary of Petitioners' Claims

Petitioners brought this lawsuit as a putative class action on behalf of approximately 400 investors (the "Investors") in a non-residential condominium luxury resort hotel known as The Registry Hotel at Pelican Bay, Naples, Florida (the "Hotel"). Investors subscribed for and purportedly purchased 474 interests in the Hotel ("Hotel Interests") pursuant to a private offering conducted by certain of Respondents (the "Offering").

During the proceedings before the District Court, Petitioners alleged that various parties who participated in the offer, financing, construction and sale of the Hotel Interests had engaged in an expansive scheme of misrepresentations, omissions and devises to defraud Investors. The primary forces behind the alleged fraudulent scheme were the underwriter of the Offering, Respondent Merrill

Lynch, Pierce, Fenner & Smith ("Merrill Lynch"), and the developer of the Hotel, Respondent Shelter Seagate Corporation ("SSG") and its shareholders and principals (the "Can-Am Respondents")[1], who collectively conceived and structured the development and financing of the Hotel and sold it to Investors.

As alleged in Petitioners' original complaint, Merrill Lynch and the Can-Am Respondents were charged with (1) violating sections 10(b) and 20(a) of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78j(b) and 78t(a); sections 12(2) and 15 of the Securities Act of 1933, 15 U.S.C. §§ 771(2) and 77o; and section 1703(a)(2) of the Interstate Land Sales Full Disclosure Act, 15 U.S.C. § 1703(a)(2); as primary violators, control persons, aiders and abettors and conspirators; (2) violating Federal and Florida RICO statutes; (3) breaching their fiduciary duties to, and contracts with, Petitioners; and (4) common law fraud and negligent misrepresentation.

C. Procedural Background

1. The District Court's Rulings

Following limited discovery, each of the Respondents filed motions to dismiss and/or motions for summary judgment as to all of Petitioners' claims. In an opinion

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[1] The Can-Am Respondents include SSG; Respondent Can-American Realty Corporation ("Can-Am Realty"), SSG's parent; Respondent Can-American Corporation ("Can-Am"), the parent of Can-Am Realty; and Respondents Garrett G. Carlson, Graham C. Lount and Arni Thorsteinson, the principal officers and/or directors of SSG, Can-Am Realty and Can-Am.

dated November 19, 1990, the District Court divided Petitioners' claims into "three claims of fraud", granted summary judgment to Respondents on the first claim, and denied summary judgment to Respondents on the second and third claims "because there may be genuine issues of material fact." (November 19, 1990 opinion at 8-9, App. 9.) Significant for purposes of this Cross-Petition was the fact that the District Court denied Respondents' summary judgment motions with respect to Petitioners' "second claim of fraud" – that Merrill Lynch and the Can-Am Respondents "fraudulently concealed their intention to lease additional furniture, fixtures and equipment on behalf of plaintiffs, and to thereby burden plaintiffs with cost overruns that defendants were contractually required to bear." (November 19, 1990 opinion at 3-4, App. 4.)

Following hearings on February 26, 1991 and March 12, 1991, the District Court ordered an expedited trial, solely of Petitioners' breach of contract claims and solely against the Can-Am Respondents. The District Court also certified a class for the sole limited purpose of the expedited trial of Petitioners' breach of contract claims against the Can-Am Respondents.[2] Relying on its authority under Fed.R.Civ.P. 16, the District Court stayed any consideration of Petitioners' remaining fraud claims pending the disposition of the expedited contract trial.

Before the expedited contract trial, Petitioners filed a Motion for Partial Summary Judgment against the Can-

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[2] The scope and binding impact of this limited class certification is the subject of the Adams Petition.

Am Respondents, asserting that, *inter alia*, SSG breached the sales contracts for each Investor's Hotel Interest by leasing significant furniture, fixtures and equipment ("FF&E") at each Investor's expense, rather than providing such FF&E to Investors free and clear, as SSG was contractually bound to do. The District Court granted summary judgment to Petitioners on the liability portion of this breach of contract claim, and held a bench trial on Petitioners' remaining contract claims against the Can-Am Respondents in May 1991.

Following the contract trial, Petitioners also filed a Cross-Motion for Summary Judgment against Merrill Lynch and the Can-Am Respondents on, *inter alia*, Petitioners' claim that Merrill Lynch and the Can-Am Respondents had committed fraud by proceeding to close the Offering despite their uncontroverted knowledge that SSG intended to lease substantial FF&E to finance construction cost overruns – in direct contravention of Respondents' contractual obligations and the representations Respondents had made to Investors (all Merrill Lynch clients) – without ever disclosing this intention to Investors. As described below, the District Court *never* addressed the factual or legal merits of this fraud claim.

On July 16, 1992, the District Court held a damage trial limited to its prior grant of summary judgment against the Can-Am Respondents for breach of contract through the leasing of FF&E. On August 7, 1992, the District Court issued its Opinion dismissing Petitioners' remaining contract claims. As to the FF&E leasing breach, the District Court awarded the plaintiff class a $6.7 million judgment (for the actual costs of the leases) against SSG, and pierced the corporate veil of SSG to impose

liability on all the Can-Am Respondents. (August 7, 1992 opinion at 43-45, App. 56.)

In its August 7, 1992 Opinion, the District Court also granted summary judgment in favor of all Respondents on all of Petitioners' fraud claims. However, the District Court declined to determine the merits of Petitioners' FF&E leasing fraud claims against Merrill Lynch and the Can-Am Respondents. Instead, the District Court concluded that, because Petitioners had been granted a $6.7 million judgment for breach of contract against the Can-Am Respondents as a result of the leasing of FF&E, Petitioners could not proceed with related tort claims against Merrill Lynch (and the Can-Am Respondents) because "there can only be one recovery for one injury." Otherwise, in the District Court's view, Plaintiffs might obtain a "double recovery" in violation of section 28(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb(a), and the common law. (August 7, 1992 opinion at 24-25, App. 34-36a.)

2. The Court of Appeals' Ruling

Petitioners appealed the District Court's "double recovery" decision on the grounds that, *inter alia*, it denied Petitioners their statutory and constitutional rights to pursue alternative, cognizable claims and to obtain judgments against all potentially liable parties (notwithstanding that Petitioners could not collect, in the aggregate, more than their actual damages). Furthermore, recognizing that the District Court had *never* addressed the merits of Petitioners' evidence offered in support of their FF&E leasing fraud claims in its August 7, 1992

opinion (even though the District Court had upheld those claims in its November 19, 1990 opinion), Petitioners identified in their Appeal Briefs substantial detailed evidence from which the ultimate trier of fact could conclude that Merrill Lynch and the Can-Am Respondents had committed fraud in connection with the leasing of FF&E. As Petitioners noted in their Appeal Briefs (and throughout their 27 volume Appendix), all of this evidence had previously been presented to the District Court in connection with both Petitioners' opposition to Merrill Lynch's and the Can-Am Respondents' Motions for Summary Judgment, and Petitioners' own Cross-Motion for Summary Judgment.

Nonetheless, the Court of Appeals affirmed the District Court's "double recovery" ruling, holding that Petitioners could not proceed with tort claims against Merrill Lynch (and the Can-Am Respondents) because Petitioners had been granted a $6.7 million judgment against SSG for breach of contract. Specifically, the Court of Appeals held:

> In addition to their breach of contract claims regarding the leasing of the disputed FF&E, the Becherer plaintiffs also brought fraud claims against SSG and Merrill Lynch arising out of the same decisions. Because it had already awarded the Becherer plaintiffs damages on the breach of contract claims, the District Court dismissed the fraud claims. According to the District Court, to do otherwise would amount to a double recovery.
>
> The Becherer plaintiffs argue that the District Court erred in dismissing their FF&E fraud claims because the dismissal prevented them

> from pursuing judgments against all potential joint and severally liable parties. The Becherer plaintiffs also argue that the measure of damages would have been different under tort and under contract.
>
> We do not find these arguments persuasive. SSG injured petitioners by leasing various FF&E that it should have provided. The District Court awarded damages to plaintiffs under a breach of contract theory and found that these damages make plaintiffs *whole*. Plaintiffs, therefore, are not entitled to recover under any tort theory, as that would result in a *windfall* to plaintiffs.

Court of Appeals opinion at 17; Adams Petition at 16a (emphasis added).

Significantly, while finding the District Court's award of damages made Petitioners "whole", the Court of Appeals reversed the District Court's decision to pierce the corporate veil of SSG to impose liability for the $6.7 million judgment on each of the Can-Am Respondents. (Court of Appeals opinion at 17-21; Adams Petition at 16-19a.) Thus, the Court of Appeals effectively concluded that Petitioners were made "whole" by the award of a judgment against only SSG, which the Court of Appeals knew to be an admittedly insolvent corporation.

The Court of Appeals also affirmed the District Court on the basis that "Plaintiffs have not provided any evidence of bad faith, as is necessary to support a fraud claim." (Court of Appeals opinion at 17; Adams Petition at 16a.) In this regard, the Court of Appeals found that:

> . . . *we have reviewed the District Court's opinions in this case and find no discussion* of when Merrill

> Lynch learned of SSG's intention to lease the disputed FF&E and whether Merrill Lynch thought that intention contravened the contract. Nor have the Becherer plaintiffs pointed to any part of the record to show they raised this argument below.

Court of Appeals opinion at 23; Adams Petition at 21-22a (emphasis added).

These statements by the Court of Appeals only serve to highlight the fact (which was overlooked by the Court of Appeals) that the District Court *never addressed* the factual or legal merits of Petitioners' FF&E leasing fraud claims, including the substantial evidence which was unequivocally proffered to the District Court by Petitioners and specifically identified in their Appeal Briefs.[3] Instead, the District Court improperly concluded that the FF&E leasing fraud claims were *moot*, because of the purportedly preclusive effect of the breach of contract judgment against SSG.

As described below, the decision by the Court of Appeals to affirm the "double recovery" ruling by the District Court not only conflicts with the decisions of this Court and numerous other United States courts of appeals, as well as fundamental concepts of joint and

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[3] Moreover, it is well settled that it is improper for a court of appeals to decide a question not reached by the district court if the decision requires consideration of facts not resolved on the record. *Tidelands Royalty B. Corp. v. Gulf Oil Corp.*, 804 F.2d 1344, 1354 (5th Cir. 1986); *Miller v. Hedlund*, 813 F.2d 1344, 1352 (9th Cir. 1987). A court of appeals does not make initial findings of fact. *See, e.g., Glover v. Johnson*, 855 F.2d 277, 284 (6th Cir. 1988).

several liability, alternative pleading and satisfaction of judgments, but also constitutes such an extreme departure from the accepted and usual course of judicial proceedings so as to deprive Petitioners of valuable property rights without due process of law, as guaranteed by the Fifth Amendment to the Constitution.

REASONS FOR GRANTING THE PETITION

A. The Court of Appeals' Decision Conflicts With the Decisions of This Court and Several Circuit Courts

This Cross-Petition is specifically limited to that portion of the Court of Appeals' opinion affirming the District Court's ruling that Petitioners are precluded under section 28(a) of the Securities Exchange Act of 1934 (and the common law) from prosecuting cognizable fraud claims against both Merrill Lynch and the Can-Am Respondents *solely* on the ground that Petitioners had been granted (as opposed to collected) a prior judgment for breach of contract against another respondent, SSG, arising out of the same wrongful leasing of FF&E. This ruling by the Court of Appeals so clearly conflicts with decisions by this Court and numerous other Circuit Courts, as well as fundamental principles of law regarding joint and several liability, alternative pleading and satisfaction of judgments, that Petitioners respectfully submit that this Court should summarily reverse the Court of Appeals, as it is authorized to do under Supreme Court Rule 16.1.

The Court of Appeals' sole basis for precluding Petitioners from proceeding with their FF&E leasing fraud

claims was its flawed reasoning that to hold otherwise would constitute a "windfall" to Petitioners, who, according to the Court of Appeals, had already been made "whole" by having been granted a breach of contract judgment for damages against SSG. (Court of Appeals opinion at 22-23; Adams Petition at App. 16a.) Not only is this reasoning legally deficient, but the Court of Appeals' conclusion that Petitioners have already been made "whole" and that Petitioners might obtain a "windfall" is also factually inaccurate since, as the District Court found, SSG is an admittedly insolvent corporation, incapable of satisfying the judgment against it. (November 24, 1992 District Court opinion at 32-33; Adams Petition at 30-31b.)

Significantly, the Court of Appeals did not cite a single case or authority in support of its decision to affirm the District Court's ruling that, as a matter of law, Petitioners could not pursue fraud claims against potentially culpable defendants because Petitioners had already been granted a judgment for damages against another (albeit impecunious) defendant – nor does it appear that it could have done so. Indeed, the Court of Appeals ignored the fact that Merrill Lynch had conceded in its own appeal brief that the District Court's decision in this regard was erroneous – obviously in recognition of the well settled law that, while a plaintiff is entitled to only one *satisfaction* of judgment, that plaintiff may still *obtain* multiple judgments, on different claims, against any culpable defendants. *See* Merrill Lynch Appeal Brief at 34, cited in Plaintiffs' Reply Brief at 24 n.29; Plaintiffs' Appeal Brief at 35.

Petitioners believe it is unprecedented for a court to preclude a plaintiff from seeking judgments from all potentially culpable defendants, simply because that plaintiff has been *granted* a monetary judgment against a single respondent – regardless of whether the plaintiff has *recovered* (or will recover) that judgment. In fact, this decision by the Court of Appeals is in direct conflict with the decisions of this Court and numerous United States courts of appeals, which have all clearly recognized that, while plaintiffs are entitled to only one satisfaction of judgment, plaintiffs are entitled to pursue alternative causes of actions and obtain judgments against multiple defendants. *See, e.g., Bigelow v. Old Dominion Copper Mining & Smelting Co.*, 225 U.S. 111, 56 L.Ed. 1009, 1023 (1912) ("if he sue one such wrongdoer and recover judgment, he is not estopped from suing another upon the same facts unless his first judgment has been fully satisfied"); *Sessions v. Johnson*, 95 U.S. 347, 349, 24 L.Ed. 596, 597 (1877) ("the rule in this country is that a judgment against one without satisfaction is no bar to an action against any one of the other wrongdoers"); *Landrigan v. City of Warwick*, 628 F.2d 736 (1st Cir. 1980); *U.S. v. Silliman*, 167 F.2d 607, 613 (3d Cir. 1948) ("it is well settled law in this country that a judgment for the plaintiff in an action against one tortfeasor acting in concert with others does not preclude the plaintiff from later suing another"); *Frank v. Volkswagenwerk, A.G. of West Germany*, 522 F.2d 321, 324-25 (3d Cir. 1975) ("a plaintiff may recover as many judgments against as many tortfeasors as he wishes, but upon *satisfaction* of one judgment, he may not sue or execute against another tortfeasor") (emphasis added); *Whitehurst*

v. Charles Town Hospital, 626 F.2d 357, 358 (4th Cir. 1980); *Reconstruction Finance Corp. v. Barrett*, 131 F.2d 745, 748 (7th Cir. 1942) ("satisfaction of one several obligation which does not discharge the whole of the liability, is not a bar to recovery from another several obligor for the same liability"); *Mclelland v. Facteau*, 610 F.2d 693, 695 n.1 (10th Cir. 1979) ("plaintiff has a separate cause of action against each defendant and is not precluded from acting against one by judgment against another"); *Gill & Duffus Service, Inc. v. A.M. Nural Islam*, 675 F.2d 404, 404-05 (D.C. Cir. 1982) ("As a rule '[t]he rendition of a judgment against one of two or more persons liable for a loss does not terminate a claim that the injured party may have against any other person who may be liable therefor' ") (quoting Restatement (Second) of Judgments § 49).

Moreover, the Court of Appeals' conclusion that Petitioners might obtain a "windfall" by obtaining judgments against multiple defendants ignored the well settled law that payments made in satisfaction of one judgment are credited against the other. *Fate v. Dixon*, 649 F. Supp. 551, 556 n.3 (E.D.N.C. 1986); Restatement (Second) of Judgments § 50(2); Restatement (Second) of Torts § 886. Thus, allowing Petitioners to pursue their FF&E leasing fraud claims against Merrill Lynch and the Can-Am Respondents would not, and could not, as a matter of law, grant them a "windfall"; payment of a judgment by one of the Respondents would have to be credited against a judgment against any other Respondent.

The Court of Appeals' ruling also effectively conflicts with Federal Rules of Civil Procedure 8(a), 8(e)(2) and 18 (allowing plaintiffs to plead and pursue as many independent and alternative claims as they may have). *See also*

Brown v. U.S., 976 F.2d 1104, 1108 (7th Cir. 1992) (Federal Rules allow parties "to pursue such alternative and inconsistent claims"); *Blazer v. Black*, 196 F.2d 139, 144 (10th Cir. 1952) (plaintiff "was at liberty to state as many separate claims as he wished"); *Tektel, Inc. v. Maier*, 813 F. Supp. 1331, 1334 (N.D. Ill. 1993) ("it is perfectly acceptable for a plaintiff to seek the same damages under different theories of recovery"). Thus, to let stand the Court of Appeals' ruling would have the chilling effect of forcing a plaintiff to determine, prior to bringing suit, which single defendant he will sue and the single legal theory pursuant to which he will sue.

The only authority cited by either the District Court or the Court of Appeals for this novel and extreme proposition is section 28(a) of the Securities Exchange Act of 1934. However, the plain language of section 28(a) is consistent with the general rule of law cited above:

> The rights and remedies provided by this title *shall be in addition to any and all other rights and remedies that may exist at law or in equity;* but no person permitted to maintain a suit for damages under the provisions of this title shall recover, *through satisfaction of judgment in one or more actions,* a total amount in excess of his actual damages on account of the act complained of. . . . (emphasis added)

While the District Court determined that this statutory language precluded Petitioners from proceeding against other defendants once Petitioners had been merely granted a judgment against one defendant (as opposed to having satisfied a judgment), there are no cases and no legislative history interpreting section 28(a)

in the restrictive manner adopted by the District Court and affirmed by the Court of Appeals. In fact, the cases dealing with section 28(a) suggest the opposite – that section 28(a) permits a plaintiff to obtain judgments under more than one cause of action arising out of the same set of facts. *See, e.g., Miley v. Oppenheimer & Co.*, 637 F.2d 318, 329-31 (5th Cir. 1981) (while section 28(a) limits recovery to "actual damages" on federal securities law claim, plaintiff also is entitled to obtain punitive damages under pendent state law claim); *Nye v. Blyth Eastman Dillon & Co.*, 588 F.2d 1189, 1200 (8th Cir. 1978) (same); *Nunes v. Merrill Lynch, Pierce, Fenner & Smith*, 609 F. Supp. 1055, 1058-60 (D.C. Md. 1985) (same).

Because the foregoing ruling by the Court of Appeals so clearly conflicts with long standing principles of law enunciated by this Court and followed by numerous other Circuit Courts, as well as with the plain language of section 28(a) of the Securities Exchange Act of 1934, Petitioners submit that this Cross-Petition for Writ of Certiorari should be granted and that the Court of Appeals should be summarily reversed pursuant to Supreme Court Rule 16.1.

B. The Court of Appeals' Decision Deprived Petitioners of Valuable Property Rights Without Due Process of Law

The Court of Appeals' ruling also constitutes such a severe departure from the accepted and usual course of judicial proceedings so as to raise a serious constitutional question as to whether Petitioners have been unlawfully deprived of property interests (the right to litigate choses

in action against Merrill Lynch and the Can-Am Respondents) without being provided substantive due process, as guaranteed by the Fifth Amendment to the Constitution.

The Court of Appeals' decision, like the District Court's decision, deprived Petitioners of their right to pursue alternative claims, and to seek to obtain judgments, against *all* potentially liable parties. *See, e.g., Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 807 (1985) ("a chose in action is a constitutionally recognized property interest possessed by each of the plaintiffs"). Moreover, the Fifth Amendment guarantees litigants a fair opportunity to present their claim if the claim has a "reasonable basis in fact or law." *Bill Johnson's Restaurants, Inc. v. NLRB*, 461 U.S. 731, 748 (1983); *Randall v. Loftsgaarden*, 478 U.S. 647, 652 (1985). Here, Petitioners' FF&E leasing fraud claims were previously acknowledged by the District Court to be reasonably based in fact and law, inasmuch as Petitioners' FF&E leasing fraud claims had survived the first wave of Respondents' summary judgment motions when the District Court found that there "may exist genuine issues of material fact" with respect to these same claims. Thus, Petitioners had a constitutional right to proceed with their well-plead FF&E leasing fraud claims against both Merrill Lynch and the Can-Am Respondents and to seek to obtain a judicial determination of the factual and legal merits of those claims.

Accordingly, in order to prevent the deprivation of Petitioners' property rights without due process of law, Petitioners respectfully request that their Cross-Petition for Writ of Certiorari be granted.

CONCLUSION

For the foregoing reasons, Petitioners respectfully request that their Cross-Petition for a Writ of Certiorari be granted.

Respectfully submitted,

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UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

RICHARD C. BECHERER, LAWRENCE MILTON RICHARD, ROBERT A. & SHIRLEY L. HORWATH, and HENRY V. & JOANN L. DENOLF, individually, and on behalf of all others similarly situated,

Plaintiffs,

v.

MERRILL LYNCH, PIERCE, FENNER & SMITH, INCORPORATED, CAN-AMERICAN CORPORATION, CAN-AMERICAN REALTY CORPORATION, SHELTER SEAGATE CORPORATION, GARRETT G. CARLSON, GRAHAM C. LOUNT, ARNI THORSTEINSON, FRANK LAVIN, MARTIN CICCO, LAVENTHOL & HORWATH, DOMINION FINANCIAL & INVESTMENT CORP., M.A. MORTENSON COMPANY and WINSOR/FARICY ARCHITECTS, INC.,

Defendants.
_____/

Case No.
89-CV-72502-DT
Hon. John Feikens

OPINION AND ORDER

(Filed Nov. 20, 1990)

This action arises out of purchases by plaintiffs of interests in a 474-room resort hotel ("Registry Hotel") to be located at Pelican Bay in Naples, Florida. Four hundred seventy-four hotel interests were sold to 298 investors, from thirty different states, for a total price of $89,225,500.

The events giving rise to this action began on or about June 15, 1982, when defendants, Can-American Corporation and/or Can-American Realty Corporation, and their principals, defendants Carlson, Lount and Thorsteinson, entered into an agreement with Westinghouse Communities of Naples, Inc. ("WCN") to purchase property for the development of the Registry Hotel. (These defendants, together with defendant, Shelter Seagate Corporation ("SSG"), are sometimes collectively referred to as "Can-Am.") At or about this time, a second developer, W.B. Johnson Company, also sought to purchase property from WCN with the intent to construct what was to become the Ritz Carlton Hotel, also to be located at Pelican Bay, Florida.

In 1983, defendant Merrill Lynch, Pierce, Fenner & Smith ("Merrill Lynch") agreed to act as the exclusive selling agent for the sale of Registry Hotel interests to potential investors. In the spring of 1983, Can-Am engaged defendant, M.A. Mortenson Company as general contractor, and defendant, Winsor/Faricy Architects, Inc., as architect, for Registry Hotel's development. Defendant Laventhol & Horwath ("Laventhol") was also retained in 1983 by Can-Am Realty to prepare a market study to

determine the feasibility of constructing the Registry Hotel and financing its development through the sale of hotel interests.

Between February 1984 and February 1985, Can-Am and Merrill Lynch marketed interests in the Registry Hotel. As part of their marketing efforts, these defendants developed and distributed a Private Placement Memorandum ("PPM") to investors and two supplements which described the investment opportunity in detail. These materials informed investors that they could cancel their purchases for any reason until they were notified that the "Minimum Subscription Level" had been met and were notified of individual financing approval. Thereafter, investors could only cancel if the hotel was not completed within two years after investors became bound.

After the offering period ended, investors' interests were "closed into escrow" on February 15, 1985. This meant that their investment funds were delivered to an escrow agent for safekeeping until the hotel was complete. When the Registry Hotel was completed, the funds would be distributed. If the Registry Hotel was not completed within two years from the date when investors became bound, investors could cancel their purchases. Various defendants represented the Registry Hotel to be "substantially complete" as of October 30, 1986, and held a final closing on that date. At this closing, the escrow was broken, investors' funds were distributed, and investors lost all cancellation rights.

These events are the background for plaintiff investors' three claims of fraud. First, plaintiffs claim that the

offering materials omitted the true identity and competitive impact of the Ritz Carlton Hotel which was subsequently built at Pelican Bay. Plaintiffs claim they were not told that this competitor hotel would be a Ritz Carlton, nor were they informed of its potential competitive impact on the Registry Hotel. Consequently, they argue, their interests are worth less than they were led to believe.

Second, plaintiffs claim that certain defendants fraudulently concealed their intention to lease additional furniture, fixtures and equipment on behalf of plaintiffs, and to thereby burden plaintiffs with cost overruns that defendants were contractually required to bear.

Third, plaintiffs claim that certain defendants fraudulently accelerated the final closing on the sale of investors' hotel interests, so that investors would be foreclosed from exercising their cancellation rights even though the Registry Hotel was not complete within the two-year time period.

I entered an order limiting initial discovery to these three fraud claims. *See* Fed. R. Civ. Pro. 16(b). The matter is now before me on defendants' motions to dismiss for failure to state fraud with particularity, as is required by Fed. R. Civ. Pro. 9(b). Pursuant to Fed. R. Civ. Pro. 56, I have converted defendants' motions to dismiss into motions for summary judgment, and for the reasons which follow, now GRANT defendants' motions for summary judgment on plaintiffs' first claim of fraud, and deny, without prejudice, summary judgment on plaintiffs' second and third claims.

Summary judgment is appropriate when "the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show that there is no genuine issue of material fact and that the moving party is entitled to judgment as a matter of law." Fed. R. Civ. Pro. 56. A "party seeking summary judgment always bears the initial responsibility of informing the district court of the basis for its motion, and identifying those portions of the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, which it believes demonstrates the absence of a genuine issue of material fact." *Celotex Corp. v. Catrett*, 477 U.S. 317, 323 (1986). Once the moving party has made this initial showing, summary judgment may follow if the non-moving party "fails to make a sufficient showing to establish the existence of an essential element of that party's case, on which that party will bear the burden of proof at trial." *Id.* at 323.

In this case, defendants, as moving parties, made the initial showing required to obtain summary judgment on plaintiffs' first fraud claim. Specifically, defendants pointed out the absence of material evidence showing that they fraudulently concealed the name "Ritz Carlton," or the potential competitive impact of the hotel on the Registry Hotel.

Plaintiffs, on the other hand, failed to make the requisite showing necessary to avoid summary judgment on their first fraud claim. To prevent summary judgment, plaintiffs, as the non-moving parties, must raise genuine issues of material fact as to all essential elements of fraud, since they bear the burden of proving these elements at trial. Elements of fraud under Securties [sic] & Exchange

Commission Rule 10b-5 or common law include materiality, scienter, reliance, causation, and injury. *See, e.g., National Bank of Detroit v. Whitehead & Kales Co.*, 528 F. Supp. 940 (E.D. Mich. 1981); *U.S. Fidelity & Guaranty Co. v. Black*, 412 Mich. 99, 313 N.W.2d 77 (1981).[1] Plaintiffs fail to raise genuine issues of material fact as to one or more of these elements in support of their first fraud claim.

First, plaintiffs raise no genuine issue of material fact regarding the alleged materiality of the name "Ritz Carlton." An omitted fact is only material if there is a substantial likelihood that a reasonable investor would consider it important in deciding whether to invest. *Basic Inc. v. Levinson*, 108 S.Ct. 978 (1988). Moreover, to fulfill the materiality requirement, "[T]here must be a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of information made available." *Id.* at 983.

In this case, the "total mix" of information given to investors included express written warnings that "additional units could be built on neighboring lands at Pelican Bay; that "a substantial competitive hotel chain has the right to build another hotel at Pelican Bay"; that, if built,

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[1] In addition to Rule 10-b5 and common law fraud, plaintiffs' securities fraud claims allege that defendants violated §12 of the Securities Act of 1933, and §1702(a) of the Interstate Land Sales Full Disclosure Act. Although these statutes may involve somewhat different elements of proof, they similarly require proof that defendants made misstatements or omissions of *material* fact. Because plaintiffs fail to make this showing on their first fraud claim, it is unnecessary to discuss these statutes in this opinion.

this hotel could "dilute the occupancy, revenues and income" of the Registry Hotel; and that it could "adversely affect the value of the [Registry] Hotel interests." PPM at 7. Because the "total mix" of information given to investors included these express warnings, a reasonable jury could not conclude that a reasonable investor would have viewed one additional piece of information – the identification of the potential competitor by the name "Ritz Carlton" – as significantly altering the total mix of investment information.

Plaintiffs also fail to raise material facts showing that investors justifiably relied on defendants' failure to identify the Ritz Carlton by name. To be actionable, an investor's reliance must be justified. *Platsis v. E.F. Hutton & Co. Inc.*, 642 F.Supp 1277. Reliance is not justified if an investor fails to exercise a minimal degree of care or due diligence in an attempt to discover readily available facts. *National Bank of Detroit v. Whitehead & Kales Co.*, 528 F.Supp. at 949; *McGraw v. Matthaei*, 388 F.Supp. 84 (E.D. Mich. 1972). As early as May 1984, investors could have readily discovered the publicly known fact that the W.B. Johnson Hotel was a Ritz Carlton. This was known well before the offering period ended, and before investors lost cancellation rights.

Plaintiffs' claims regarding the occupancy and revenue projections also fail. First, projections of this sort are not material unless they are capable of being calculated with substantial certainty. *James v. Gerber Products Company*, 587 F.2d 324, 327 (6th Cir. 1978). Plaintiffs offer no material facts showing that occupancy and revenue projections for the Registry Hotel could have been calculated with substantial certainty. In fact, it is uncontroverted

that the PPM stated the contrary. It included such warnings as: "Some assumptions inevitably will not materialize. Therefore, the actual results achieved during the projection period will vary. The projected statements should not be relied upon to indicate actual results." PPM at 67. Because the offering materials contained these unambiguous warnings, investors cannot now claim that these projections were material to their investment decision.

However, even if these original projections were material and misleading, or became so once defendants knew that the Ritz Carlton was actually under construction, they were adequately revised to reflect the Ritz Carlton's competitive impact well before investors lost their general cancellation rights; and thus investors cannot now claim they reasonably relied on the original projections.

Investors were given the revised occupancy and revenue projections in a supplemental PPM issued on October 31, 1984. They could cancel their purchases for any reason until they received notice that the "Minimum Subscription Level" had been met, and received notice that they were approved for financing (*see* PPM at p. 44). These requirements were fully satisfied no earlier than February 15, 1985, at the escrow closing. Accordingly, investors had more than three months to consider whether they should cancel their purchases based on the new projections. Having failed to exercise their cancellation rights during this period, investors cannot now claim that they reasonably relied on the original projections, even assuming those projections were materially misleading.

For these reasons, defendants' motion for summary judgment is GRANTED on plaintiffs' first fraud claim, and defendant Laventhol is DISMISSED since it is not encompassed by the remaining claims. Because there may be genuine issues of material fact on plaintiffs' second and third fraud claims, defendants' motion for summary judgment on those claims is DENIED without prejudice.

Additionally, with the following exceptions, all other motions to dismiss are DENIED without prejudice. Remaining for consideration are: (1) motions to dismiss for lack of personal jurisdiction as to defendants Cicco, Lavin, Lount, and Thorsteinson; (2) motions to dismiss based on failure to satisfy the applicable statutes of limitations; (3) motions by Carlson, Shelter Seagate, and Can-Am to dismiss Counts XV and XVI of the Complaint for failure to state a cause of action for breach of contract or warranty; and (4) motion by plaintiffs for class certification.

These motions will be considered at the next hearing. Specifically, I will consider: (1) whether defendants Cicco, Lavin, Lount, or Thorsteinson had "minimum contacts" with the State of Michigan, thereby subjecting them to this court's jurisdiction; (2) whether any of plaintiffs' claims are time-barred; (3) whether plaintiffs have adequately stated a cause of action for breach of contract or warranty; (4) whether defendants need to conduct discovery on plaintiffs' remaining fraud claims; (5) the propriety of treating plaintiffs' second fraud claim – concerning the allegedly fraudulent leasing – as a breach of contract claim; and (6) plaintiffs' motion for class certification.

The next hearing is scheduled for Friday, December 7, 1990, at 1:30 p.m., 858 Federal Building and United States Courthouse, Detroit, MI 48226.

/s/ John Feikens
John Feikens
United States District Judge

Dated: Nov 19, 1990

UNITED STATES DISTRICT COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

RICHARD C. BECHERER, LAWRENCE MILTON RICHARD, ROBERT A. HORVATH and SHIRLEY L. HORVATH, and HENRY V. DENOLF and JOANN L. DENOLF, individually, and on behalf of all others similarly situated,

Plaintiffs,

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MERRILL LYNCH, PIERCE, FENNER & SMITH, INCORPORATED, CAN-AMERICAN CORPORATION, CAN-AMERICAN REALTY CORPORATION, SHELTER SEAGATE CORPORATION, GARRETT G. CARLSON, GRAHAM C. LOUNT, ARNI THORSTEINSON, FRANK LAVIN, MARTIN CICCO, LAVENTHOL & HORWATH, DOMINION FINANCIAL & INVESTMENT CORP., n/k/a TRUSTBANK MORTGAGE CENTER, INC., M.A. MORTENSON COMPANY, WINSOR/FARICY ARCHITECTS, INC., and MIDWEST TITLE GUARANTY COMPANY OF FLORIDA,

Defendants.
_____/

Civil Action
No. 89-72502
Hon. John Feikens

OPINION

(Filed Aug. 7, 1992)

I. Background

This case began with a lengthy complaint containing sixteen counts. It alleged that a group of 298 investors, who asked to be designated as a class, purchased unit interests in a 474-room resort hotel (The Registry Hotel), herein referred to as "the hotel," to be located on Pelican Bay in Naples, Florida, for a total price of $89,225,500. Named as defendants are a group, referred to herein as "the developer," Can-American Corporation, Can-American Realty Corporation, Shelter Seagate Corporation, Garrett G. Carlson, Graham C. Lount, and Arni Thorsteinson. Also named as defendants are Merrill Lynch, Pierce, Fenner & Smith, Inc.; Frank Lavin; Martin Cicco; Laventhol & Horwath, certified public accountants retained by the developer; Dominion Financial & Investment Corporation; M.A. Mortenson Company; and Winsor/Faricy Architects, Inc.

The counts captioned in the complaint are:

1. Violation of the Exchange Act, § 10(B) and Rule 10b-5;
2. Violations of the Exchange Act, § 20;
3. Violations of the Securities Act, § 12(2);
4. Violation of the Securities Act, § 15;
5. Fraudulent and negligent misrepresentation;
6. Violation of the Land Sales Act;
7. Aiding and abetting/conspiracy;

8. Violation of RICO;

9. Violation of Florida's RICO statute;

10. Breach of fiduciary duty (against named defendant[s]);

11. Breach of fiduciary duty (against named defendant[s]);

12. Breach of fiduciary duty (against named defendant[s]);

13. Malpractice/negligence;

14. Respondeat superior;

15. Breach of warranty; and

16. Breach of contract.

In managing this case, I concluded that there was a strong need for the adoption of special procedures, since the case involved complex issues, multiple parties, and difficult legal questions (Fed.R.Civ.P. 16(c)(10)).

The complaint was filed on August 21, 1989, and there followed a blizzard of motions and briefs. Between August 21, 1989 and April 23, 1990, the date on which the court was able finally to schedule a Rule 16 conference, there were ninety docket entries, comprised of discovery motions, Rule 12 and 56 motions, and supporting and response briefs.

Clearly, Rule 16 had to be vigorously applied.

A pretrial conference held on April 23, 1990 began this process. With close questioning of parties' counsel, it appeared that the complaint was bottomed on allegations

of fraud and breach of contract. Three occurrences of fraud were alleged:

1. That the Private Placement Memorandum (the "PPM"), which disclosed that the W.B. Johnson Company was interested in erecting a hotel on Pelican Bay, did not say that that hotel was a Ritz-Carlton;

2. That the PPM stated that the hotel was to be furnished with approximately $13.5 million of furniture, fixtures and equipment; and that defendants, or some of them, rather than perform that contractual undertaking, leased the furniture, fixtures and equipment placed in the hotel and thereby burdened the hotel with lease payments; and

3. That fraud surrounded the October 31, 1986 closing date, when the hotel was to be "substantially completed."

That status conference on April 23, 1990, as the record amply demonstrates (*see* Appendix A), compacted the prolix allegations of fraud in the complaint to three manageable areas and, on May 15, 1990, a detailed order managing initial discovery was entered.

In motion hearings, these three occurrences were then addressed.

In an Opinion and Order dated November 20, 1990, I granted a motion for summary judgment on plaintiffs' first fraud claim. I found no fraud in the claim that the investors were not notified that another hotel to be built on Pelican Bay would be a Ritz-Carlton hotel. That Opinion, and the resulting Order, sets forth the reasons for the

grant of summary judgment and is attached hereto as Appendix B.

On March 15, 1991, I entered an Order for an expedited trial. I determined that the remaining two issues of alleged fraud could be tried as breach of contract claims against the developer Shelter Seagate, Can-American Corporation, Can-American Realty Corporation, and the individual defendants Carlson, Lount and Thorsteinson (referred to collectively as "the Shelter Seagate Group", or as "SSG", or as "the developer"). In that Order I also certified a plaintiff class (attached hereto as Appendix C). Jury trial was waived.

On the second claimed issue of fraud, reformed into a breach of contract claim, *i.e.*, the decision by the developer-defendants to lease furniture, fixtures and equipment for the hotel rather than to purchase them, resulted, following a full hearing, in a grant of partial summary judgment in favor of the plaintiff class and against the developer-defendants. That ruling was made on May 7, 1991. A transcript setting forth the reasons and grounds for that grant of partial summary judgment is contained in Appendix D attached hereto, the transcript being a record of the ruling made on that date. I reserved for a future hearing a determination of the remedy for that breach.[1]

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[1] That hearing has now been held and damages have been determined. *See infra.*

II. Breach of Contract Claim

In this section, the third issue, reformed as a breach of contract claim, is addressed.

The trial parties are the plaintiff class and the Shelter Seagate defendants, the developer.

Beginning in February, 1984, the plaintiff class ("the investors") entered into contracts with defendant Shelter Seagate Corporation ("SSG") for the purchase of "Hotel Units" in The Registry Hotel. Investors paid at least 10% of the purchase price as a cash down payment and applied for mortgage financing for the remainder. SSG agreed to deposit investors' down payments, notes, and executed mortgages with a designated escrow agent until construction of the Hotel Units was "substantially completed" and the sale was closed. Investors were free to cancel their purchase agreements until (1) they were approved for financing, and (2) they received notice from SSG that the "Minimum Subscription Level" had been attained. Thereafter, investors were "irrevocably bound" to complete their purchases.

SSG agreed, however, that if they did not "substantially complete" the hotel, and close the sale of Hotel Units, within two years from the date that investors became "irrevocably bound," investors would be given the option of rescinding their contracts with a return of all deposits, or demanding specific performance by SSG.

On October 31, 1986, SSG represented to the escrow agent that the hotel was substantially complete and that it had complied with all conditions precedent to closing the

sale. The escrow agent agreed, released investors' funds ($89,225,500) from escrow and closed the sale.

In August of 1989, nearly three years later, six investors brought this lawsuit, individually and on behalf of nearly 300 similarly situated investors, seeking to rescind their contracts with SSG.

On March 15, 1991, I entered an Order scheduling an expedited trial on plaintiff class' contract claims and certifying a plaintiff class (Appendix C, *supra*). In that Order, I limited the expedited trial to deciding plaintiffs' class claims against the "Shelter Seagate Group" defendants, since that was the group with which the plaintiff class had contracted. I pointed out that, if there were breaches of contract, such issues could be tried in far less time and "would avoid unnecessary costs of trial." Plaintiff class filed an amended complaint stating breach of contract claims, but expressly reserved the right to litigate their fraud claims in the future.

The expedited trial addressed this issue: Whether SSG, by closing the sale of Hotel Units to the investors, breached its agreement to *substantially complete* the hotel within two years from the date investors became bound.[2]

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[2] The expedited trial was held in May, 1991. The apparent anomaly between my ordering an expedited trial and the delay in issuing this Opinion is explained by noting that all the parties to this lawsuit were negotiating a global settlement during the intervening period, and indeed did reach such a settlement. However, under the terms of the settlement, the number of plaintiff class members who elected to opt out of the proposed settlement was sufficient to scuttle the agreement.

A. Findings of Fact

Between February, 1984, and April, 1985, plaintiff class entered into contracts with SSG for the purchase of Hotel Units in The Registry Hotel, a non-residential, luxury condominium resort complex which SSG planned to develop at Pelican Bay in Naples, Florida. Each Hotel Unit cost between $179,500 and $278,000 and included a fully furnished hotel room or suite, a percentage interest in the hotel's common areas, and a percentage interest in the hotel's future profits. Plaintiff class appointed SSG as their agent, authorizing it to rent hotel units, collect pool revenues, pay operating expenses, and distribute cash dividends to plaintiff class at regular intervals.

Prior to making their purchases, investors (herein also known as "plaintiff class") were given a Private Placement Memorandum (PPM) which described the offering in detail. In the PPM, investors were advised that Hotel Units were business investments with distinct tax shelter benefits. As long as investors used their units for not more than 14 days in any taxable year, the units were considered business investments for tax purposes. As such, under the tax laws then in effect, investors were entitled to claim yearly tax deductions based on the "depreciation" value of their units, and for any interest on mortgage financing. To the extent that depreciation and interest deductions for any taxable year exceeded the investors' share of the hotel's Net Operating Income, an investor would realize a tax "loss" which could be off-set against income from other sources, thus producing tax savings. In short, investors were aware that even if the hotel performed poorly during its first years of operation,

the investment was beneficial as a mechanism for sheltering other income from taxation.

Testimony at trial demonstrated that the tax shelter aspect of this investment was a significant factor in enticing the investors to purchase hotel units. This is highlighted by the fact that the PPM and its supplements devoted a considerable amount of space to the tax consequences of the investment. Because the tax shelter aspect was a significant factor in this investment, the alleged under-performance of the hotel, of which the investors now complain, would have benefited them by providing greater tax losses to off-set against their other income.

Notably, the tax shelter laws changed shortly after the instant sale was closed. Under the new laws, investors are no longer entitled to off-set Registry Hotel losses against their other income. This materially diminishes the tax benefits of plaintiff class' purchases.

The purchase agreement between SSG and each member of plaintiff class is set forth in a document entitled "Unit Sale Agreement," and in other documents incorporated by reference therein. Pursuant to paragraph 2 of the Unit Sale Agreement, investors agreed to pay SSG a cash down payment equaling at least 10% of the purchase price, and agreed to apply for mortgage financing for the remainder. SSG agreed to place down payments, mortgages, and notes in an escrow account with a designated escrow agent, to be held until SSG fully satisfied the conditions precedent to closing the sale.

The following provisions of the Unit Sale Agreement controlled SSG's right to close the sale:

Paragraph 4 states:

> ***Completion Date.*** Seller shall substantially complete construction of the Hotel not more than two years after this Agreement becomes binding on the Purchaser as such two year period may be extended under the Interstate Land Sale Full Disclosure Act.

Paragraph 5 states:

> ***Closing of Title.*** The closing of title shall be held within a reasonable time after completion of construction of the Hotel Unit, at the office of the escrow agent. . . .

Paragraph 8 states:

> ***Default.*** Seller shall be in default hereunder if Seller fails to close the sale pursuant to Section 5 within two years after this Agreement becomes binding on Purchaser, as such two year period is defined in the federal Interstate Land Sale Full Disclosure Act and the regulations and guidelines promulgated thereunder. Purchaser's remedy against Seller for Seller's default hereunder shall be either to obtain a refund of all deposits made pursuant hereto (together with interest earned thereon, if any) whereupon this Agreement and the parties' rights hereunder shall terminate, or to seek specific performance of this Agreement, at the Purchaser's election.

Exhibit B to the Escrow Agreement (incorporated by reference into the Unit Sale Agreement) is entitled "Closing Requirements" and denominates those conditions that had to be satisfied before the sale closing could take place. Exhibit B provides in relevant part:

> The requirements for closing or escrow and title under the Agreement and the applicable contract [identified as the Unit Sale Agreement], which must first be completely satisfied or met are:
>
> 2. Receipt of Developer's written assignment of all existing warranties, books and records of the condominium owners association, plans, specifications, and all certificates or permits obtained or required with respect to the construction, occupancy and operation of the Hotel, to the condominium owners association and to the Purchaser, as appropriate.

I find that investors became "irrevocably bound" to complete their purchases on February 15, 1985, the day their funds were delivered into escrow by SSG, and that SSG therefore had until February 15, 1987 to substantially complete the hotel and close the sale. Because SSG elected to close the sale on October 31, 1986, I find that SSG waived whatever time remained in the two-year completion period and obligated itself to deliver a substantially complete hotel by the closing date, October 31, 1986. *See* Appendix D (Transcript of May 7, 1991 hearing).

Photographic, documentary and testimonial evidence of the physical and operational condition of the hotel on or about October 31, 1986, the date of the closing of sale and title, demonstrated that the hotel was not substantially complete at that time. Heavy construction was proceeding on the top floors of the hotel; some rooms on the top floor had no walls while others had metal studs; some rooms in the hotel lacked carpeting, wall coverings, and furniture, fixtures and equipment; on some floors, metal studs and drywall were just being erected. There was an

absence of fully assembled furniture from the top floors down through floors 4 and 5, and any furniture that was present was in boxes or stacked throughout the rooms and in the corridors. The ballrooms, restaurants, nightclub and commercial areas of the hotel were still in an incomplete state of construction on the date of the sale closing.

On the closing date, SSG had not obtained all certificates necessary to operate the hotel. It had obtained a partial certificate of occupancy and a partial certificate of fire compliance, but these certificates were predicated on SSG's assurance that no guests would be allowed in the hotel. Similarly, although SSG had obtained an Architect's Certificate of Substantial Completion, this certificate was limited to the work of the general contractor, and did not pertain to the entire hotel.

After the October 31, 1986 closing, construction and finishing work continued. On December 2, 1986, Deputy Fire Chief Rodgers issued a Notice of Fire Compliance which permitted guests to occupy certain limited areas of the hotel, including the rooms on floors 3-14. On December 5-6, 1986, the hotel received its first guests, a meeting of the Naples Board of Realtors. At that time, one of the hotel's three restaurants was open; the nightclub, Garrett's, was not open. Approximately 50-75 guest rooms were used during the weekend of December 5-6, 1986. On or about December 15, 1986, 24 more guest rooms on floors 3-11 were made available. In early January, 1987, there was a function for approximately 75-100 investors at the hotel. In March, 1987, the hotel hosted a large gathering of "meeting planners" with approximately

150-200 overnight guests. By that time the hotel was substantially complete.

Plaintiff class retained Phillip Levin, a management consultant, to determine whether the hotel lost money due to the delay in substantial completion. Levin testified that he (1) reviewed the financial statements of The Registry Hotel for December, 1986, and the quarterly statements for 1987 to ascertain the hotel's performance during these periods; (2) reviewed SSG's projections in the PPM and supplements thereto to determine how the developer predicted the hotel would perform; (3) reviewed the performance of competitive hotels in the Naples area to see how they performed during this period; (4) reviewed the economy in Naples during that period of time; and (5) reviewed the reputation of The Registry Hotel Corporation which was managing the hotel for SSG.

Levin testified that the hotel under-performed during the first quarter of 1987 because it only achieved a 53% occupancy rate. He testified that it should have achieved a 72% occupancy rate during this period, given the strong demand for hotel rooms in the area (Levin noted that the Ritz Carlton Hotel at Pelican Bay was 100% occupied during this period), and given the competent management of the Registry staff. Levin testified that the hotel did not perform as he would have expected for one of two reasons. "Either the rooms weren't available for the guests, or guests for some reason chose not to stay at this hotel." He concluded that because of the delay in substantial completion, and attendant construction problems, the hotel was unable to attract the number of guests it

otherwise could have. Based on Levin's analysis, plaintiff class claims an aggregate loss of over $7 million.

Levin's testimony was contradicted by several witnesses. Philip Wood, a guest on December 5 and 6, 1986, testified that his stay at the hotel was very pleasant. Terri Autrey and Jim Knauff of the Registry's sales staff testified that no prospective guest, group or transient, was turned away during this period.

Moreover, sales figures for the hotel show that its gross revenues for the first five months of 1987 were $11,850,000, while gross revenues for the same months of 1988 were $13,357,000. The relative similarity of these figures suggests that if the hotel did "under-perform" in 1987, it also under-performed in 1988, at a time when it was substantially complete. In fact, the hotel actually generated more revenue in January of 1987 ($2,039,070), when it was not substantially complete, than it did in January of 1988 ($1,877,649), when it was. These facts negate plaintiff class' argument that the hotel lost money in 1987 due to the delay in substantial completion.

Levin conceded that he did not compare The Registry Hotel's performance during its first months of operation to the performance of other local hotels, such as the Ritz Carlton, during their first months of operation.

I find that Levin's testimony is not credible. His analysis is based on assumptions that are not adequately supported by factual data and was refuted by the testimony of Registry sales staff.

B. Conclusions of Law

This court's jurisdiction and venue over the subject matter of this trial are based on Section 27 of the Securities Exchange Act of 1934; the federal securities law subject matter of the original complaint, as amended by the First Amended Complaint (for breach of contract); ancillary and pendent jurisdiction; and the court's Opinion and Order dated December 14, 1990.

The Shelter Seagate Group defendants, through SSG, entered into a series of contracts with each member of the plaintiff class for the sale of one or more Hotel Units in The Registry Hotel. The terms and conditions of the agreement are contained in Unit Sale Agreements executed between plaintiff class and SSG, and the documents incorporated therein by reference. Pursuant to paragraph 19 of the Unit Sale Agreement, the agreement is to be construed according to Florida law.

Pursuant to paragraph 1 of the Unit Sale Agreement, SSG agreed to sell and convey, and plaintiff class agreed to purchase, fully furnished, non-residential resort condominium Hotel Units of The Registry Hotel at Pelican Bay, including an appurtenant interest in the income-producing Commercial Units of the hotel, percentage ownership interest in fee simple in the land on which the hotel is situated and the other common elements of the hotel, and a management agreement appointing SSG as the agent of the Hotel Unit Purchaser to manage and operate such Hotel Units and investors' undivided interest in the Commercial Units as part of the hotel.

Pursuant to paragraph 4 of the Unit Sale Agreement, defendants agreed to substantially complete construction

of each Hotel Unit not more than two years after each Unit Sale Agreement became binding on purchasers "as such two year period may be extended under the Interstate Land Sales Full Disclosure Act."

Pursuant to paragraph 20 of the Unit Sale Agreement and page 42 of the PPM, I found that the agreement became binding on purchasers on February 15, 1985, the date their down payments, mortgages, and notes were closed into escrow. I found that defendants thus had until February 15, 1987 to substantially complete the hotel, but waived that right by electing to close on October 31, 1986. In order to comply with paragraph 4 of the Unit Sale Agreement, the hotel had to be substantially complete by October 31, 1986.

Pursuant to paragraph 5 of the Unit Sale Agreement, defendants agreed to "complete" construction of the hotel before closing the sale. I find that the word "complete" means "substantially complete" when read together with paragraphs 4 and 8 of the Unit Sale Agreement. Therefore, I find that in order to comply with paragraph 5 of the Unit Sale Agreement, defendants had to substantially complete the hotel prior to closing the sale.

Substantial completion of the hotel meant that the Unit Owners could utilize the property in accordance with its intended use, *i.e.*, a working business ready to be occupied and used by guests and to generate rent. *See J.M. Beeson Co. v. Sartori*, 553 So.2d 180 (Fla.App. 4 Dist. 1989).

Plaintiff class has the burden of proving that the hotel was not substantially complete at the time of closing on October 31, 1986, and that they were damaged

thereby. SSG has the burden of proving that, in the event the hotel was not substantially complete as of October 31, 1986, their breaches of contract were not material. *See* Transcript of May 7, 1991 hearing.

As a result of closing the sale of the hotel on October 31, 1986, defendants breached the contract in the following manner.

Paragraph 4 of the Unit Sale Agreement was breached because on October 31, 1986, the hotel was not capable of use for its intended purpose, *i.e.*, a working business ready to be occupied by guests, and therefore was not substantially complete within two years after each investor's Unit Sale Agreement became binding.

Paragraph 5 of the Unit Sale Agreement was breached because defendants closed title prior to substantially completing construction of the Hotel Unit.

Paragraph 2 of Exhibit B to the Escrow Agreement ("Closing Requirements") was breached because defendants failed to obtain by closing date all "certificates or permits . . . required with respect to the construction, occupancy and operation of the hotel."

These conclusions lead inevitably to the question: How were the members of the plaintiff class damaged?

I conclude that plaintiff class did not carry their burden of proving that they were damaged as a result of the aforementioned breaches. In a case such as this, where the damages claimed are lost profits, plaintiff class cannot rely on speculation and conjecture, but must prove with reasonable certainty the amount of their actual loss. *Royal Typewriter Co. v. Xerographic Supplies,*

719 F.2d 1092 (11th Cir. 1983). *See, also, Beverage Canners, Inc. v. Cott Corp.*, 372 So.2d 954, 956 (Fla.Dist.Ct.App.1979). Additionally, plaintiff class must prove with reasonable certainty that their damages "flowed as the natural and proximate result of the claimed breach." *See Royal Typewriter*, 719 F.2d at 1105 (quoting *Aldon Industries, Inc. v. Don Myers & Associates, Inc.*, 517 F.2d 188, 191 (5th Cir. 1975).

This, plaintiff class cannot do, as I point out in my findings of fact. Florida law, which governs this dispute, recognizes two methods of proving lost profits: (1) the before-and-after theory and (2) the yardstick test. *See G.M. Brod & Co. v. U.S. Home Corp.*, 759 F.2d 1526, 1539 (11th Cir. 1985). The before-and-after theory requires a comparison between the profits generated by a business before and after the claimed breach. *Id.* at 1536. The yardstick test consists of a study of the profits of business operations that are closely comparable to plaintiff class' to determine whether plaintiff class indeed lost profits as a result of the claimed breach. *Id.* Here, there is a lack of comparability; and, since the estimates depend on too many variables, plaintiff class cannot rely on the yardstick rule, as they have not met their burden of showing lost profits to a reasonable degree of certainty. *See, supra, Beverage Canners*, 372 So.2d at 956; *Royal Typewriter*, 719 F.2d at 1105.

Application of the "before-and-after" test to this case requires a comparison of the hotel's performance during its first few months of operation (when it was not substantially complete) and its performance during an analogous subsequent period (when it was substantially complete). Defendants presented evidence at trial which

showed that the hotel generated $11,850,000 in revenues for the first five months of 1987, and $13,357,000 for the first five months of 1988, a difference of only $1,507,000. It was also shown that the hotel actually generated more revenue in January, 1987 than it did in January, 1988. This evidence refutes plaintiff class' claim that the hotel's poor performance in 1987 was due to the delay in substantial completion.

Plaintiff class similarly fails to prove lost profits under the so-called "yardstick" test. Plaintiff class' expert, Levin, compared The Registry Hotel's actual performance during its first months of operation with the performance of other luxury hotels in and around Naples during the same months, and found that hotels such as the Ritz Carlton were 100% occupied while The Registry Hotel was only 53% occupied. He concluded that given the obvious local demand for luxury hotel rooms, The Registry Hotel should have achieved a minimum occupancy rate of 72% in the first quarter of 1987. Its failure to do so, he concluded, was due to either the lack of available rooms or to the fact that The Registry Hotel was not in "first class" condition at the time.

Levin's assessment was refuted by Registry hotel staff persons who testified that no prospective guest was turned away during this period for lack of available rooms. Levin's analysis also fails to give sufficient weight to The Registry Hotel's status as a newcomer to the local market. In order to assess whether The Registry Hotel actually under-performed during its first months of operation, Levin should have compared The Registry's initial performance with the initial performance of other luxury hotels in the Naples area.

For example, if Levin had shown that the Ritz Carlton's initial performance significantly exceeded The Registry Hotel's initial performance, and that both opened under similar market conditions, he may have come considerably closer to raising an inference that The Registry Hotel significantly under-performed during its early months. He would still have to show that the under-performance was due to the delay in substantial completion, and not to other possible factors, such as poor management by Registry staff. Based on the testimony adduced at trial, I find that Levin did not present sufficient evidence to make the latter finding.

Because plaintiff class has not shown that they were damaged by defendants' breach, and defendants have shown that the breach is not material, plaintiff class is not entitled to either rescission or damages. "It is elementary that the mere breach of an agreement which causes no loss . . . will not sustain a suit for damages, much less rescission." *See, e.g., Burger King v. Mason*, 710 F.2d 1480, 1489-90 (11th Cir. 1983) (quoting *Block v. City of West Palm Beach*, 112 F.2d 949, 952 (5th Cir. 1940). Plaintiff class argues that paragraph 8 of the Unit Sale Agreement gives them an unqualified right to rescission. I do not agree. As the U.S Court of Appeals for the Eleventh Circuit stated:

> [A]lthough as a general rule parties to a contract may strictly enforce its [termination] terms, and the courts will not rewrite an agreement to undo the consequences of a bad bargain, *see, e.g., Sapienza v. Bass*, 144 So.2d 520 (Fla.Dist.Ct.App. 1962), the Florida Courts do not blindly sanction unilateral termination of contracts when a default causes no harm to the party seeking to avoid performance.

Burger King, 710 F.2d at 1490.

The hotel which plaintiff class purchased may not be as profitable as they expected, nor the tax shelter they envisioned, but that is an investment risk they knowingly took. This court will not relieve them of a bargain they now consider unwise.

C. Summary

I conclude that the SSG defendants breached their contracts with plaintiff class by closing the sale of Hotel Units to the investors before the hotel was substantially complete. However, because plaintiff class had no ascertainable economic loss as a result of defendants' breach, plaintiff class is not entitled to damages or to rescission.

III. Fraud Claims Against Merrill Lynch and Shelter Seagate – Motions To Dismiss and For Summary Judgment

Plaintiff class alleges three fraud claims against Merrill Lynch and SSG pursuant to Rule 10b-5 of the Securities Exchange Act, common law fraud, and negligent misrepresentation. In addition, plaintiff class alleges that Merrill Lynch, SSG, Mortenson, and Winsor/Faricy violated the Land Sales Act. These allegations are now addressed in response to motions to dismiss and for summary judgment.

A. Complete v. Substantially Complete Fraud Claim

Plaintiff class claims that Merrill Lynch and SSG made material misrepresentations of the requirements for

closing of title. They allege that Merrill Lynch and SSG represented to the investors that the hotel had to be *fully completed* prior to closing. In support of this fraud claim, they point to the Private Placement Memorandum, Merrill Lynch Marketing Guide, and affidavits of former Merrill Lynch sales agents.

The short answer to this claim is that I have already held that the Unit Sale Agreement only required SSG to substantially complete the hotel prior to closing. These defendants could not have defrauded the investors by representing the transaction could only be closed upon the complete completion of the hotel because they, in fact, represented the opposite, that the closing could occur upon substantial completion.

Plaintiff class nevertheless points to the PPM, and argues that it states the closing would not occur until the hotel was completely complete. The PPM says no such thing. Page 3 of the PPM states that the "closing of the sale of the Hotel Interests is subject to various conditions including completion of the Hotel. . . . " However, this statement falls under the heading "MEMORANDUM SUMMARY," which indicates reference should be made to the table of contents for direction to more detailed information in the body of the memorandum. The table of contents, under "closing of sale," directs the reader to page 42. Page 42 of the PPM makes only an oblique reference to the degree of completeness required prior to the closing, but it is telling: "After all required funds and documents have been deposited with Escrow Agent, the deed for Investor's Hotel Unit from SSG to Investor . . . shall be recorded and . . . copies of . . . the Architect's Certificate of Substantial Completion . . . shall

be forwarded to Investor, which will complete the closing of the sale as far as the Investor is concerned."

Plaintiff class next points to the 79 form affidavits they submitted that essentially say that if each investor had discovered prior to the closing that SSG was only required to substantially complete the hotel, each would have terminated his or her subscription. However, when the plaintiff class signed Unit Sale Agreements, they did indeed "discover" what the requirements were regarding completeness, since paragraph 4 contains the operative "substantially complete" language.

Plaintiff class also claims that these defendants, through the Merrill Lunch sales representatives, orally misrepresented that the closing could not occur unless the hotel was completely complete. Plaintiff class ignores the fact that the Unit Sale Agreement they signed contains a merger and integration clause (paragraph 13), stating explicitly that the purchaser acknowledges he or she has not relied on any other representations made by the seller or seller's agent; and that the PPM, in bold letters, states that oral representations cannot be relied upon, and that any representation not contained in or beyond the statements in the PPM is made without authority. *See Acme Propane, Inc. v. Tenexco, Inc.*, 844 F.2d 1317 (7th Cir. 1988) (oral statements are irrelevant if adequate written disclosures are given prior to closing).

Last, I point out again that even though I find there was no fraud in the representations made as to the closing requirements regarding completeness, I have already held that the breach of contract in this regard in no way damaged the plaintiff class. I conclude that there is no

evidence whatever of fraud in the closing of the sale of the hotel, even though the hotel was not substantially complete at that time.[3]

Accordingly, motions to dismiss and for summary judgment as to these claims must be granted.

B. Purchase v. Lease FFE Fraud Claim

Plaintiff class claims that Merrill Lynch and SSG materially misrepresented to investors that SSG would purchase the furniture, fixtures, and equipment ("FFE") for the hotel, when both knew that SSG intended to lease certain FFE items. They allege that this conduct violated Rule 10b-5 of the Securities Exchange Act, common law fraud, and negligent misrepresentation.

On May 7, 1991, I granted partial summary judgment in favor of plaintiff class on the breach of contract issue. (*See* Appendix D). I found, as a matter of law, that SSG breached its agreement to convey a fully furnished hotel to investors. A hearing, in order to determine damages for that breach, was held on July 16, 1992. A discussion of those damages in [sic] found in Section VIII. of this Opinion.

The FFE fraud claim is not cognizable. Under both the securities law and state common law there can only be one recovery for one injury. In this case, plaintiff class was awarded damages for SSG's breach of the agreement

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[3] Plaintiff class' other fraud allegations against the defendants are equally unavailing and do not merit further discussion.

to convey a fully furnished hotel to investors. They cannot now claim additional damages for the same injury.

Section 28(a) of the Securities Exchange Act, 15 U.S.C. §78bb(a), prevents a party from receiving double recovery for a security law violation. That section provides:

> The rights and remedies provided by this chapter shall be in addition to any and all other rights and remedies that may exist at law or in equity, but no person permitted to maintain a suit for damages under the provisions of this chapter shall recover, through satisfaction of judgment in one or more actions, a total amount in excess of his actual damages on account of the acts complained of.

Similarly, the common law fraud and negligent misrepresentation claims are also not cognizable because a party is only entitled to one recovery for one injury. That is:

> A plaintiff who alleges separate causes of action is not permitted to recover more than the amount of damage actually suffered. There cannot be double recovery for the same loss even though different theories of liability are alleged in the complaint. Thus, a plaintiff who recovers the full amount of damages for the breach of contract cannot recover damages in tort unless he alleges and proves the existence of additional damages attributed solely to the tort.

22 Am.Jur. 2d, Damages §35. *See also Kewin v. Mass. Life Ins. Co.*, 79 Mich.App. 639, 653; 263 N.W.2d. 258, 265 (1977), *aff'd in part and rev'd in part on other grounds*, 409 Mich. 401, 295 N.W.2d. 50 (1980) ("If a plaintiff seeks to

recover in both contract and tort, he may not recover the same damages under both theories.")

This is not a case where plaintiff class is entitled to additional damages. Even if the FFE fraud claim was cognizable, plaintiff class is not entitled to rescission or punitive damages. Rescission is not an appropriate remedy where, as here, the remedy at law is adequate. 37 Am. Jur. 2d, Fraud and Deceit §323, §325. Similarly, punitive damages are only allowed where the alleged fraud is malicious, deliberate, gross, or wanton fraud in this case.

Thus, since plaintiff class will recover damages for the breach of contract claim with respect to FFE, they cannot recover damages pursuant to the securities law, common law fraud, or on negligent misrepresentation theories of liability. Thus, the FFE fraud claims must be dismissed on both motions to dismiss and for summary judgment.

C. Rule 10b-9 and 15c2-4 Fraud Claim

Plaintiff class claims that Merrill Lynch violated Rule 10b-9 and 15c2-4 of the Securities Exchange Act, by allowing the closing of title to take place on October 31, 1986 despite their knowledge that all conditions for closing were not met.

They argue that Rules 10b-9 and 15c2-4 require a broker participating in a distribution, in which payments are not to be made until certain events or contingencies occur, to take specific steps to ensure that the issuer does not receive any funds from investors until all contingencies are fully satisfied. Here, they claim that these rules

require Merrill Lynch to ensure that investors' funds were not released from escrow until all closing requirements were met, including completion of the hotel.

Plaintiff class misconstrues the applicability of these rules. They relate to "all or nothing" or "part or nothing" offers. According to the terms of an "all or nothing" offering, if within a specified period there is not a full subscription to all shares being offered, the offer is cancelled. Similarly, in a "part or nothing" offering, a refund will be made to subscribers if less than a specified portion of the offering has been subscribed to. Thomas Lee Hazen, *Treatise on the Law of Securities Regulation* § 6.3, at 273 (2d Ed. 1990).

Rule 10b-9 provides that an issuer entering into one of these types of offerings must be specific as to the offering price, duration of the offer, and the amount of the securities that must be sold to make the offering effective, or the offering is considered a "manipulative or deceptive device" in violation of Section 10(b) of the Securities Exchange Act. Rule 15c2-9 provides that it is unlawful for a broker or dealer to engage in these offers unless the funds are placed into a separate bank account until all relevant contingencies have occurred, *i.e.*, the minimum subscription level is met.

Thus, Rules 10b-9 and 15c2-4 protect investors' funds when securities are sold subject to a minimum sales condition. Merrill Lynch satisfied these rules on February 15, 1985, when the minimum sales conditions were met and the escrow was closed, thus irrevocably binding the investors. The conduct that plaintiff class claims violated these rules occurred at or near the October 31, 1986

closing of title. Rule 10b-9 and 15c2-4 do not apply to Merrill Lynch's conduct, which occurred after the February 15, 1985 closing of escrow. Thus, plaintiff class' Rule 10b-9 and 15c2-4 fraud claim must be dismissed on Merrill Lynch's motion to dismiss.

D. Land Sales Act Claims

In their complaint, plaintiff class alleges a violation of the Federal Interstate Land Sales Act ("Land Sales Act" or "the Act"), 15 U.S.C. § 1701, *et seq.* The Land Sales Act, section 1703(a)(2), makes it unlawful for any developer or agent to defraud to deceive a purchaser with respect to the sale of any non-exempt lot. Plaintiff class also alleges a violation of section 1707 for the failure to provide them with a property report prior to their signing of the Unit Sale Agreements and prior to their receipt of the deeds at the closing of sale and title on October 31, 1986.

Defendants assert that sale of the Hotel Units is exempt from the Land Sales Act under section 1702(a)(2), which provides that the Act does not apply to "the sale or lease of land under a contract obligating the seller or lessor to erect [a residential, commercial, condominium, or industrial] building thereon within a period of two years." Thus, the sale of the Hotel Units is exempt from the Land Sales Act if SSG is obligated to complete the hotel within two years of the sale of the units.

Plaintiff class argues that the two-year period begins to run when the sale of the hotel interests occurred, and that the sale occurred when the purchasers signed the Unit Sale Agreements. But case law provides that the two-year period during which the seller must complete

the building begins when the contract becomes legally binding upon both parties.

The U.S. Housing and Urban Development ("HUD") Guidelines provide that the section 1702(a)(2) exemption requires the seller to finish the building within two years from the date the purchaser signed the contract. *Guidelines for Exemptions Available Under the Interstate Land Sales Full Disclosure Act*, 44 Fed. Reg. 24,010, 24,012 (April 23, 1979). However, HUD Guidelines equate "signing" the contract with "entering a contract and incurring an obligation" for purposes of this exemption.

In *Winter v. Hollingsworth Properties, Inc.*, 777 F.2d 1444, 1449 (11th Cir. 1985), the court held that "for the purposes of the ILSFDA [Land Sales Act] the 'sale' takes place at the time the purchaser signs the contract *and incurs an obligation.*" (emphasis added). *See also Markowitz v. Northeast Land Co.*, 906 F.2d 100, 104 (3rd Cir. 1990). ("[F]or the purposes of the Act the sale occurs when the purchaser signs the sale agreement and incurs an obligation.")

The position that the time of the "sale" for purposes of the Land Sales Act is the time the contract becomes legally binding is also supported by a reasonable construction of other provisions of the Act. Under section 1703(b), the purchaser can revoke the sale of a lot within 7 days of the signing of the contract. In addition, under section 1703(c), the purchaser can revoke the sale up to two years after the signing of the contract if the Act is violated. The phrase "signing of the contract" means the time that the purchaser becomes legally bound, or these revocation provisions would be meaningless.

In this case, paragraph 4 of the Unit Sales Agreement provides that:

> Delivery of the hotel units will be made no more than two years after the Investor's subscription for his hotel units becomes binding as such two year period is defined in the Federal Land Sales Full Disclosure Act and the regulations promulgated thereunder.

Plaintiff class signed the Unit Sale Agreements between February and October of 1984. These agreements did not become legally binding until February 15, 1985, when the investors became irrevocably bound according to the terms of the Unit Sale Agreement. Because neither party was legally bound under the Unit Sale Agreements until February 15, 1985, there was no "sale" for the purposes of the Land Sales Act until that date. Because the Unit Sale Agreement obligated the Seller SSG to erect the hotel within two years of that date, this transaction is exempt from the Land Sales Act. Thus, plaintiff class' Land Sales Act claims must be dismissed.

IV. Contract Claims Against Merrill-Lynch – Motions To Dismiss

Plaintiff class' First Amended Complaint raises two contract claims against Merrill Lynch. First, they allege that Merrill Lynch violated an implied covenant of good faith and fair dealing. Specifically, they claim that Merrill Lynch breached this covenant by wrongfully closing units into escrow on February 15, 1985 before the investors

received notice of their mortgage approval from Dominion Financial & Investment Corp. (n/k/a Trustbank Mortgage Center, Inc.), and by wrongfully closing title on October 31, 1986 because SSG had not substantially completed the hotel.

The implied covenant of good faith and fair dealing is not applicable in this case. It applies only "where a party to a contract makes the manner of its performance a matter of its own discretion". *Burkhardt v. City National Bank*, 57 Mich. App. 649, 652; 226 N.W.2d 678 (1975). Where the contract itself defines the manner of performance, the performance is not subject to the implied covenant of good faith and fair dealing. *General Aviation, Inc. v. Cessna Aircraft*, 703 F.Supp. 637 (W.D. Mich. 1988), *aff'd in part and rev'd in part on other grounds*, 915 F.2d 1038 (6th Cir. 1990).

In this case, Merrill Lynch did not exercise any discretion with respect to closing the units into escrow on February 15, 1985. The Unit Sale Agreement outlined the conclusions that had to be met before investor funds could be released into escrow. Because Merrill Lynch did not have discretion regarding the performance of his agreement, the implied covenant of good faith and fair dealing is not applicable. The same reasoning applies with regard to the closing of title on October 31, 1986. It was Midwest Title Guaranty Company of Florida ("Midwest Title"), the escrow agent, who performed the duties related to the closing of title. Merrill Lynch did not exercise discretion in performing duties related to the closing of title. Thus, the implied covenant of good faith and fair dealing contract claim is dismissed.

Second, plaintiff class alleges that Merrill Lynch entered into a joint venture with SSG, making it vicariously liable for their breaches of contract. The elements of a joint venture are:

1. An agreement reflecting an intention to engage in a joint venture;
2. a joint undertaking of;
3. a single project for profit;
4. a sharing of profits as well as losses;
5. a contribution of skills or property by the parties; and
6. a community of interest in and control over the subject matter of the enterprise.

Pinnacle Port Community Association v. Orenstein, 872 F.2d 1536, 1539 (11th Cir. 1989) (Fla. law). *See also Meyers v. Robb*, 82 Mich. App. 549, 557; 267 N.W.2d 450 (1978).

I hold that there was no joint venture betwen Merrill Lynch and SSG. Where the parties' agreement is embodied in a written contract, the parties' intent is determined from that contract. *Hyman v. Regenstein*, 258 F.2d 502, 512 (5th Cir. 1958) (Fla. law), *cert. denied*, 359 U.S. 913 (1959). *See also Moore v. Campbell Foundry*, 142 Mich. App. 363, 367; 369 N.W.2d 904 (1988). The agency agreement between Merrill Lynch and SSG does not indicate any intent on the part of either party to form a joint venture. To the contrary, the clear and unambiguous intent of the agency agreement is to make Merrill Lynch the exclusive sales agent of the offering. There is no evidence of an agreement between Merrill Lynch and SSG reflecting an intention to engage in a joint venture. Thus, the joint

venture contract claim against Merrill Lynch is dismissed on its motion.

V. Claims Against Trustbank Mortgage Center – Motion For Summary Judgment

Plaintiff class argues they have adequately alleged and submitted evidence to support their claims of separate, independent tort and contract actions against Dominion Financial & Investment Corp., n/k/a/ Trustbank Mortgage Center, Inc., ("TMC"). TMC has moved for summary judgment on plaintiff class' original complaint and first amended complaint.

A. Contract Claims

Plaintiff class contends that a contractual obligation existed between them and TMC regarding how and when the escrow would be closed. Pursuant to the Unit Sale Agreement and the PPM, each investor agreed to apply for financing with TMC for the purchase of his or her hotel interest. Accordingly, each investor submitted a mortgage loan application to TMC. To this point, plaintiff class' argument is sound. However, they then take a remarkable leap and assert that pursuant to the PPM, TMC agreed that it would not fund investors' mortgage loans until such time as all the closing requirements set forth in the PPM and escrow agreement were fully satisfied. What is missing, of course, is any allegation that TMC was a contractual party to the PPM or escrow agreement. They were not; and the leap from the mortgage loan applications and loan commitments – where TMC

was a contractual party – to the PPM and escrow agreement – where TMC was not a contractual party, is one of faith only, and one that this court is unwilling to make[4].

B. Tort Claims

Plaintiff class also asserts they have valid claims against TMC for the torts of securities fraud, Land Sales Act fraud, common law fraud, negligent misrepresentation and conversion. The Land Sales Act fraud claim as to all defendants has already been addressed and dismissed. As for the remaining claims, there are equally insurmountable obstacles to plaintiffs' recovery, and I now turn my attention to the principal one, the *D'Oench, Duhme* doctrine[5].

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[4] Plaintiff class also charges TMC with liability under a "joint venture" theory, but fails to produce any evidence of an agreement to share profits or a duty to share losses, nor any evidence that TMC exercised joint control over the project, two of the four elements necessary to establish a "joint venture." *Pinnacle Port Community Association, Inc. v. Orenstein*, 872 F.2d 1536 (11th Cir. 1989).

[5] In addition to the *D'Oench* bar, plaintiff class' 10b-5 claim must fail because TMC's funding of investors' loans in October 1986 was not undertaken "in connection with" the sale of plaintiff class' investments, which was completed at the February 1985 escrow closing, *see Opinion and Order*, dated November 19, 1990, pp. 3 and 8; plaintiff class' common law fraud and negligent misrepresentation claims must fail because all of the investors (who are part of the plaintiff class, and to whose depositions I was cited) testified they did not base their investment decision on representations made by TMC. *See* Horvath dep., pp. 38-40; Denolf dep., pp. 70-72; Richard dep., pp. 27-29; Becherer dep., pp. 19-22. Nor did TMC have any legal duty to assure the plaintiff class a completed hotel; and plaintiff class'

C. The D'Oench Duhme Doctrine

Simply put, *D'Oench* and its progeny completely bar plaintiff class' claims against TMC. In *D'Oench, Duhme v. FDIC*, 315 U.S. 447 (1942), a borrower gave a promissory note to a bank, but received no loan in return. The parties orally agreed the bank would not enforce the note. When the bank failed, the Federal Deposit Insurance Corporation ("FDIC") acquired the note and attempted to enforce it. The borrower defended on the basis of lack of consideration. The U.S. Supreme Court held the borrower could not raise this defense against FDIC because the "secret agreement" was not part of the bank's records. The Court held as a matter of public policy that FDIC must be able to rely on a bank's records to make quick, accurate evaluations of a bank's financial condition. *See Langley v. FDIC*, 484 U.S. 86 (1987). This ability is essential to properly regulate and safeguard the nation's banking system[6]. *Id.*

The *D'Oench* doctrine bars borrows form asserting virtually any claim arising out of agreements not appearing in a contract the bank executed and maintained in its records. *See Beighley v. FDIC*, 868 F.2d 776 (5th Cir. 1989). The doctrine applies whether or not the borrower

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conversion claim must fail because it is merely a warmed-over breach of contract claim.

[6] In January, 1991, the Resolution Trust Corporation ("RTC") became the conservator of TMC's parent corporation, and by operation of law succeeded to all of the parent's right, title and interest in the investors' notes. 12 U.S.C. §§ 1821(d)(2)(A) and 1441a(b)(4). RTC was appointed receiver of TMC's parent corporation in March, 1992.

intended to deceive banking authorities or acted in good faith. *See FDIC v. Investors Associates X*, 775 F.2d 152 (6th Cir. 1985). The doctrine even applies if the bank examiners had notice of the alleged agreement prior to taking control of the bank. *See Hall v. FDIC*, 920 F.2d 334 (6th Cir. 1990). Finally, the doctrine applies to agreements made with bank subsidiaries, such as TMC, as well as with those made with banks themselves. *See Astrup v. Midwest Federal Savings Bank*, 886 F.2d 1057 (8th Cir. 1989); *Victor Hotel v. FCA Mortgage Corp.*, 928 F.2d 1077 (11th Cir. 1991).

Plaintiff class' claims all rely on representations, omissions, agreements and/or undertakings allegedly emanating from sources outside of TMC's express contract documents, and therefore fall squarely within the *D'Oench* prohibition. There is no express, written agreement establishing TMC's involvement with a "joint venture." *See Savers Federal Savings & Loan Assn. v. Amberley Huntsville*, 934 F.2d 1201 (11th Cir. 1991). Therefore, this claim must fail.

Neither is there an express, written agreement between TMC and investors (now the plaintiff class) regarding "how and when the escrow would be closed." Investors here rely on the PPM and the escrow agreement, agreements to which TMC was not a party. They also argue that TMC has within its records numerous documents (such as credit applications, sales materials, offering documents, construction loan documents, etc.) that, "when viewed together, will satisfy the requirements . . . and/or eliminate *D'Oench* 'secret' agreement considerations." *Plaintiffs' Combined Cross-Motion for Summary Judgment and Response to Defendants' Motions To Dismiss and Motions for Summary Judgment*, pp. 117-118. However,

the obligations allegedly flowing from these documents are not clearly evidenced in any express, written agreement, as *D'Oench* requires, but at best can only be inferred[7]. These claims must therefore fail as well. *See Beighley*, 868 F.2d at 784; *Bell & Murphy and Assoc. v. Inter First Bank Gateway, N.A.*, 894 F.2d 750 (5th Cir. 1990), *cert. denied*, 111 S.Ct. 244 (1990); *Fair v. NCNB Texas National Bank*, 733 F.Supp. 1099, (N.D. Tex. 1990).

Plaintiff class' fraud claims can be easily dispensed with as well. They all boil down to a contention that TMC falsely warranted the hotel as complete when it funded the investor loans. However, such a representation nowhere exists on any TMC contract. In *Hall, supra*, the plaintiffs had obtained a loan to finance the construction of a motel. A dispute arose, and plaintiffs sued the bank for breach of the loan agreement, alleging the bank's funding of the loan constituted a representation that the terms of the loan agreement had been satisfied. The U.S. Court of Appeals for the Sixth Circuit held that the plaintiffs were precluded from "presenting proof of any representations made by [the bank] beyond the terms of the loan agreement." *Hall*, 920 F.2d at 338. *See also Beighley*,

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[7] Plaintiff class also argues that such an express, written document may exist in TMC's records, but that they have been given insufficient discovery to unearth it. This claim is simply incredulous. Plaintiff class' *first* request for production of documents asked TMC to produce any agreement to provide funding to the hotel, any document regarding TMC's determinations on the completion of the hotel, and any documents relating to the funding of investors' loans which occurred in October, 1986. If such an agreement existed, plaintiff class would have already found it. Additional discovery would be futile and repetitive. *See FSLIC v. Cribbs*, 918 F.2d 557, (5th Cir. 1990).

supra; Langley, supra; FDIC v. Cardinal Oil Well Servicing Co., Inc., 837 F.2d 1369 (5th Cir. 1988); *FSLIC v. Lafayette Investment Properties, Inc.*, 855 F.2d 196 (5th Cir. 1988)[8].

In an effort to salvage their tort claims against TMC, plaintiff class argued at the June 25, 1992 hearing, and in their most recent brief, that *D'Oench* is inapplicable because TMC tortiously converted, by fraud or theft, plaintiff class' mortgages and notes from escrow, and thus never acquired legal title to the instruments. Plaintiff class argued that when TMC funded the investors' mortgages in October 1986, it really was not funding those mortgages; that, instead, it was fulfilling an agreement it had to take out SSG's construction loan with a permanent loan. Plaintiff class asserted at the June 25, 1992 hearing that they had in their possession an express, written TMC document evidencing this scheme. I gave them an additional two weeks to produce this document for my inspection; but, it now appears that no such document exists. In the absence of such a document, their conversion claim still relies on alleged misrepresentations, omissions, side agreements and/or conspiratorial undertakings between TMC and other defendants that render plaintiff class' notes and mortgages something

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[8] Plaintiff class' claims for secondary fraud liability against TMC must likewise fail, *see Investors X, supra; FDIC v. Dixon*, 681 F.Supp. 408 (E.D.Mich. 1988); *Bohm v. Forum Resorts, Inc.*, 762 F.Supp. 705 (E.D. Mich. 1991), as must plaintiff class' breach of fiduciary duty claim, *see Schlifke v. Seafirst*, 866 F.2d 935 (7th Cir. 1989); *Clay v. FDIC*, 934 F.2d 69 (5th Cir. 1991); *Timberland Design v. First Service Bank for Savings*, 932 F.2d 46 (1st Cir. 1991).

other than what they appear to be – a claim clearly barred by *D'Oench*, no matter how labeled.[9]

Accordingly, TMC's motions for summary judgment on plaintiff class' original complaint and First Amended Complaint must be granted.

VI. Winsor/Faricy Architects, Inc. and M.A. Mortenson Company

Plaintiff class' claims against both Winsor/Faricy and Mortenson must be stayed[10] to permit arbitration pursuant to Sections 2 and 3 of the Federal Arbitration Act, 9 U.S.C. §§ 2-3. If, as plaintiff class alleges, they are direct third-party beneficiaries of both the construction contract between SSG and Mortenson, and the architect contract between SSG and Winsor/Faricy, they are bound as a matter of law by the arbitration clauses contained in those respective contracts (Article 16.1 of the construction contract and Article 9.1 of the architect contract). *See Morrie Mages and Shirlee Mages Foundation v. Thrifty Corp.*, 916 F.2d 402 (7th Cir. 1990); *Interpool Limited v. Through Transport Mutual Ins. Assoc. Ltd.*, 635 F.Supp. 1503

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[9] Even if the notes and mortgages were not "assets" because of TMC's allegedly tortious conversion, *D'Oench* would still apply. *See First State Bank of Wayne County, Kentucky v. City and County Bank of Knox County, Tennessee*, 872 F.2d 707 (6th Cir. 1989); *Bowen v. FDIC*, 915 F.2d 1013 (5th Cir. 1990); *Royal Bank of Canada v. FDIC*, 733 F.Supp. 1091 (N.D.Tex. 1990); *Hall, supra*, 920 F.2d at 339 ("The doctrine may therefore be invoked even where FDIC does not have 'an interest in an asset.' ")

[10] To the extent plaintiff class is an intended third-party beneficiary of these contracts and to the extent any claims survive this Opinion.

(S.D.Fla. 1985); *Laborers International Union of North America v. HSA Contractors, Inc.*, 728 F.Supp. 519 (E.D.Wis. 1989). Thereafter, if necessary, this court may review and confirm, modify, correct or vacate the arbitrators' award. 29 U.S.C. §§ 9-11.

VII. Midwest Title Guaranty Company Motion

Midwest Title Guaranty Company of Florida ("Midwest") has moved to drop itself as a misjoined party, while plaintiff class has moved to join Midwest as a defendant. The circumstances surrounding these motions are as follows. When this litigation began in August, 1989, Midwest was not a named defendant. I issued the Order authorizing plaintiff class to file an amended complaint on January 7, 1991. That Order did not authorize plaintiff class to add additional party defendants, nor did plaintiff class seek leave from this court to add Midwest. Nevertheless, in plaintiff class' amended complaint, Midwest was named as a defendant.

Plaintiff class argues that they properly added Midwest as a defendant without an order of this court pursuant to Federal Rule of Civil Procedure ("FRCP") 15(a), which provides:

> A party may amend the party's pleading once as a matter of course at any time before a responsive pleading is served. . . .

However, they admit that at least one responsive pleading had been served by the time their amended complaint was filed. There is no alternative but to hold that Midwest was not properly joined pursuant to FRCP 15(a).

Plaintiff class next argues they are entitled to add Midwest pursuant to FRCP 21, which provides:

> Parties may be dropped or added by order of the Court on motion of any party or of its own initiative at any state of the action and on such terms as are just. Any claim against a party may be severed and proceeded with separately.

I disagree with plaintiff class' argument. Plaintiff class added Midwest to their amended complaint in violation of FRCP 15(a); without leave of this court as required by FRCP 21; and in contravention to my January 7, 1991 Order. Furthermore, they knew as early as April, 1991 that Midwest objected to being added as a defendant, yet took no corrective action until May, 1992. At this stage of the litigation it would simply be unjust to add Midwest as a defendant. This case is nearly three years old, and the paperwork submitted thus far has surely decimated a small forest. Nothing suggests the claim against Midwest is newly discovered; indeed, an escrow closing is a normal part of any real estate transaction. Last, the claims against Midwest, if any remain viable after this Opinion, are discrete and severable. *See Michaels Building Co. v. Ameritrust Co.*, 848 F.2d 674 (6th Cir. 1988).

Accordingly, Midwest's motion to be dropped as a misjoined party must be granted, and plaintiff class' motion to join Midwest as a defendant must be denied.

VIII. Damages Resulting From Breach of FFE Agreement

As discussed above, I have already found as a matter of law that SSG breached its agreement to convey a fully

furnished hotel to the plaintiff class. A hearing was held July 16, 1992, to determine the amount owed plaintiff class due to this breach.

A. The Measure of Damages

1. Plaintiff Class' Position

Plaintiff class argues first that they are entitled to rescission; next, that they are entitled to "benefit of the bargain" damages; and, last, that they are entitled to their out-of-pocket expenses.

I find that rescission is totally unwarranted as a remedy. Damages amounting to approximately $6.7 million is an adequate remedy, both in fact and in law. *See Seaside Community Development Corp. v. Edwards*, 573 So.2d 142 (Fla.App. 1 Dist. 1991).

Plaintiff class next argues for "benefit of the bargain" damages, starting that that amount is "reflected by the diminution in value of the Hotel resulting from Defendants' breach. . . . " They contend that the diminution in value of the hotel is "most appropriately measured based on Laventhol & Horwath's April 1987 Market Study of the Hotel, which shows actual cash flow for the Hotel's first four months of operation, reflects Defendants then most recently revised and reduced projections for the Hotel (dated December 4, 1986) and contains a specific line item which expressly establishes, for the first time, the actual impact that leasing of FF&E had (and would have) on cash flow." *Plaintiffs' Trial Brief In Support Of Claim For Damages*, pp. 7, 9.

Even if I were to agree that members of the plaintiff class are entitled to "benefit of the bargain" damages, this approach is completely insupportable. The cash flow projections of the hotel were revised in December 1986 for a whole host of reasons unrelated to the leasing of FFE (such as increased competition, the impact of the new tax laws, and the effects of an overall economic slowdown); and, therefore, trying to figure a value based on those projections is totally inappropriate. However, plaintiff class is not entitled to "benefit of the bargain" damages, in any event. They have not shown the defendants acted in bad faith, merely that they breached their contract. *See Cook v. Deltona Corporation*, 753 F.2d 1552 (11th Cir. 1985); *Howard v. Metcalf*, 487 So.2d 43 (Fla.App. 2 Dist. 1986). This now leaves out-of-pocket damages.

2. Defendants' Position

Defendants agree that members of the plaintiff class are only entitled to their out-of-pocket lease costs, but argue they are entitled to various off-sets that reduce that amount significantly. Defendants' position essentially, is that they are entitled to restitution for amounts they paid for additions to the hotel, additions to the pre-opening budget, etc., because they were under the mistaken belief that they could off-set those amounts by leasing, rather than purchasing, significant FFE. In other words, defendants want restitution because they spent extra sums on the hotel, believing they could recoup those amounts by breaching their contract with the plaintiff class. For obvious reasons, this claim cannot survive. *See Section 51 of the Restatement of Restitution, Comment A; Naugle v.*

O'Connell, 833 F.2d 1391 (10th Cir. 1987).[11] Again, this leaves out-of-pocket damages.

B. Out-Of-Pocket Damages

Plaintiff class' expert, J. Stanley Blumin, testified that the total out-of-pocket expense paid, and to be paid, under the leases defendants entered into on behalf of plaintiff class (the MDFC, Mellon, Denrich, B&W, Pitney Bowes and Nothern [sic] Telecom leases) is $5,161,136.09. Plaintiff class is entitled to these expenses.

Defendants' only serious objection was that the Northern Telecom lease should not be included because the PPM allowed defendants to lease a television and a phone for each hotel unit. However, that is exactly the rub. The PPM allowed defendants to lease *a phone*, while the Northern Telecom lease was for the guts of the hotel

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[11] Defendants also claim they are entitled to off-sets for leases signed after October 31, 1986, the date the Agency Agreement became effective; for leases for equipment "commonly leased" in the hotel industry; and for the tax benefits plaintiff class received as a result of the leasing. All of these arguments are unavailing. Although the timing of leases is important, it is not controlling. The mere fact that defendants leased certain FFE *after* the Agency Agreement became effective does not change the fact that the FFE was required to be purchased as part of the price plaintiff class paid for the hotel. Likewise, I find that defendants, despite their protestations, had no authority to enter into leases for equipment "commonly leased" in the hotel industry. Last, any tax benefits accruing to the plaintiff class as a result of this breach are entirely speculative. Such passive losses are only allowed to be off-set against passive gains; and, because the hotel is losing money, it is unlikely any investor has been able to make use of this potential tax savings.

phone system, i.e., for the computer equipment and software that made the phones in each unit work. That, clearly, was not meant to be the subject of a lease agreement, and plaintiff class is entitled to recover the costs of that lease as well.

Blumin also testified that plaintiff class had lost $1,290,930.47 in interest income that would have been earned had no lease payments been required and the monies been invested instead. Plaintiff class is likewise entitled to this amount.

In addition, Blumin testified that the plaintiff class was damaged in the amount of $281,158, due to lost investment tax credits. Unlike the earlier discussion regarding passive losses that could have been used to offset passive gains (if any), these tax credits are a direct credit against taxes owed. I merely need to assume that each investor earned some income and paid some taxes in order to find this an appropriate component of plaintiff class' damages, and I do exactly that. Accordingly, plaintiff class is entitled to this amount as well.

Last, Blumin testified that the plaintiff class was damaged because they had to borrow operating expenses to run the hotel. He stated that if the lease payments had not been made, the availability of that money would have obviated the need to borrow and saved plaintiff class $696,183 in interest. While in and of itself this may be true, plaintiff class is now trying to double-dip. That is, if the money paid on the leases had been available to them, they could have either invested it, and earned the $1,290,930.47 discussed above, or they could have used it for operating expenses, saving the $696,183 of the interest

incurred; but they could not have done both. Accordingly, this portion of plaintiff class' claimed damages is disallowed.

To summarize, plaintiff class is entitled to $5,161,136.09 in damages for the actual lease payments, $1,290,930.47 in damages for lost interest income, and $281,158.00 in damages for lost investment tax credits. The total damage award is $6,733,224.56.

Finally, I conclude that Can-Am Corporation, Can-Am Realty Corporation, Garrett G. Carlson, Graham C. Lount, and Arni Thorsteinson are secondarily liable for SSG's breach of contract regarding the wrongful leasing of hotel furniture, fixtures, and equipment. These entities and individuals, referred to as "the Shelter Seagate Group," improperly held themselves out to investors as the developer of The Registry Hotel, capable of fulfilling SSG's contractual obligations. Because SSG was a mere instrumentality of these individuals and entities, and because these individuals and entities improperly held themselves out to investors as capable of fulfilling SSG's contractual obligations, they are liable for any damage caused by SSG's breach of contract. *See, e.g., Dania Jai-Alai Palace, Inc. v. Sykes,* 450 So.2d 1114 (Fla. 1984).

IX. Conclusion

I reiterate that this case, with its many ramifications, presented me with numerous challenges. Now that my work is completed, I am sure that the need for conferencing and scheduling mandated by Fed.R.Civ.P. 16, and utilized here, was of utmost importance. For, when the issues were compacted into manageable questions and I

addressed the various motions that the parties had filed, each came into much clearer perspective.

X. Orders

For clarity's sake, the various Orders that are required to carry out the conclusions of law reached in this Opinion are serialized in this final section. Reference in a respective Order to the opinion on which it is based is contained in each individual Order. Where appropriate, the prevailing parties may submit proposed Judgments.

/s/ John Feikens
John Feikens
United States District Judge

Dated: August 7, 1992

Supreme Court, U.S.
FILED
SEP 6 1995
CLERK

No. 95-44

In The

Supreme Court of the United States

October Term, 1995

RICHARD C. BECHERER, et al.,

Cross-Petitioners,

v.

J. DON ADAMS, MERRILL LYNCH, PIERCE, FENNER & SMITH, INCORPORATED, et al.,

Cross-Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

BRIEF IN OPPOSITION TO CROSS-PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

I.

Whether the Petition should be denied because the Court of Appeals did not make the ruling on which Petitioners seek review.

II.

Whether the Petition should be denied because Petitioners do not seek review of the Court of Appeals' holding that Petitioners failed to produce evidence of fraud by Merrill Lynch, which is an independent ground for affirmance.

III.

Whether the Petition should be denied because the Court of Appeals' holding that Petitioners failed to produce evidence of fraud by Merrill Lynch is not appropriate for review by this Court.

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COUNTER-STATEMENT OF THE CASE

1. INTRODUCTION

Petitioners are disappointed investors in a luxury resort hotel in Naples, Florida who launched broad attacks against all parties involved with the investment, only to come up short when required to offer evidence. The Petition is limited to the claim that Merrill Lynch, the sales agent for the Hotel offering, and Shelter Seagate Corporation ("SSG"), the developer, failed to disclose to Petitioners that SSG would, after the completion of the Hotel offering, breach its contract with Petitioners by leasing certain furniture, fixtures and equipment rather than purchasing it (the "FF&E fraud claim").

Five and one-half years of litigation involving two complaints, extensive discovery and motion practice and a partial trial produced a massive, 28-volume appellate appendix. After reviewing this record, the Court of Appeals, in a unanimous opinion authored by Judge Cornelia Kennedy and joined in by Judges Damon Keith and Richard Suhrheinrich, correctly held that Merrill Lynch was entitled to judgment as a matter of law on the FF&E fraud claim because Petitioners "have not provided any evidence of bad faith, as is necessary to support a fraud claim." 43 F.3d 1054, 1064.

The Petition does not seek review of this ruling. Petitioners only seek review of the *District Court's* ruling that they could not pursue the FF&E fraud claim against Merrill Lynch because Petitioners had obtained a judgment for breach of contract against SSG (the so-called "one recovery" ruling). (Statement of Questions Presented; Petition pp. 2, 11). Petitioners incorrectly attribute

this ruling to the Court of Appeals and also incorrectly represent this to be the "sole basis" for the Court of Appeals' decision. (Petition at 11-12.)

The Petition should be denied because the one recovery ruling was not part of the Court of Appeals' opinion. Further, the Petition does not challenge the Court of Appeals' holding that Petitioners failed to prove an essential element of their fraud claim. The Petition's failure to challenge this independent ground for affirmance is fatal. Finally, the Court of Appeals' holding that Petitioners failed to produce evidence of fraud is not appropriate for review by this Court.

2. PROCEDURAL BACKGROUND AT THE DISTRICT COURT

A. The FF&E Fraud Claim

Petitioners alleged that subsequent to the closing of the hotel offering, SSG breached its contract by leasing FF&E which it was contractually obligated to purchase from the offering proceeds. They claimed Merrill Lynch was liable for fraud because before the offering closed, they alleged, Merrill Lynch knew SSG intended to lease FF&E but intentionally concealed that from Petitioners.

B. Petitioners' Factual Submission

In the summer of 1990, at the direction of the District Court, Petitioners conducted discovery on their fraud claim and then filed a brief and supporting evidence purporting to establish a *prima facie* case of fraud. While

the Petition asserts that discovery was "limited", Petitioners' counsel received thousands of Merrill Lynch documents, deposed every Merrill Lynch witness that they sought, and ultimately assured the District Court that they had the discovery needed to establish their *prima facie* case. (July 24, 1990, Hearing Transcript, pp. 6-7.)

C. Merrill Lynch's Initial Motion for Summary Judgment

Merrill Lynch and SSG responded to Petitioners' factual submission with their own, seeking summary judgment on the FF&E leasing claim. The private placement memorandum for the offering disclosed that certain FF&E would be leased. SSG submitted evidence that at the time of the closing of the offering, it did not intend to lease the kitchen and laundry FF&E.[1] Merrill Lynch filed uncontradicted deposition testimony and documents which established that prior to closing, when SSG proposed leasing additional FF&E for the kitchen and laundry areas, Merrill Lynch reduced and restructured its fees to eliminate that need. As a result, when the offering closed, Merrill Lynch understood that this FF&E would *not* be leased.

---

[1] In addition, SSG proffered evidence that when it later leased the FF&E, it did so in good faith based upon the documents and two legal opinions.

D. The November 19, 1990 Opinion

On November 19, 1990, the District Court issued an opinion on the pending motions. With respect to the FF&E fraud claim, the Court ruled:

> Because there *may* be genuine issues of material fact on plaintiffs' second and third fraud claims [including the FF&E fraud claim], defendants' motion for summary judgment on those claims is DENIED *without prejudice*.

799 F. Supp. 755, 783 (emphasis added).

E. The District Court's Recognition That Breach of Contract Is The Core Of The FF&E Fraud Claim

At the next conference, the District Court recognized that alleged breaches of contract by SSG were the core of the fraud claims. Petitioners agreed that breach of contract was "basically the essence of the case" (December 7, 1990 Hearing Transcript, p. 4). The court therefore deferred consideration of the remaining fraud claims pending an expedited, bifurcated trial on the contract claims against SSG.

F. The District Court's Ruling That Petitioners Had No Contract Claims Against Merrill Lynch

Petitioners then filed an Amended Complaint asserting contract claims against Merrill Lynch on theories of "joint venture" and "breach of the duty of good faith". After Merrill Lynch moved to dismiss, the District Court

held that Petitioners had no contract claims against Merrill Lynch and scheduled the contract claims against SSG for trial. (March 12, 1991 Hearing Transcript, p. 5; March 15, 1991 Order).

G. The SSG Contract Claims

The day before trial, the District Court held that SSG breached its contract with investors by leasing FF&E and granted summary judgment against SSG on liability. After a bench trial on damages, it awarded Petitioners $6.7 million in damages, which represented all of the lease payments and lost tax credits, plus interest. 799 F. Supp. at 777.

H. Renewal Of Merrill Lynch's Summary Judgment Motion

Merrill Lynch renewed its motion for summary judgment on the FF&E fraud claim. As a result of the bench trial, the District Court had an extensive factual record – the original 1990 fact submissions, summary judgment motions and documents, the trial testimony and exhibits, and additional materials filed with the renewed summary judgment motions.

I. The August 7, 1992 Opinion

The District Court's August 7, 1992 opinion dismissed all remaining claims against Merrill Lynch. On the FF&E fraud claims, the District Court held that because Petitioners had been awarded damages for SSG's breach,

they could not recover additional damages for the same injury.

3. THE COURT OF APPEALS' OPINION

The Petition incorrectly asserts that the Court of Appeals affirmed the District Court "solely on the ground that" Petitioners had been granted a $6.7 million judgment against SSG for breach of contract. (Petition, pp. 11-12). When the Court of Appeals intended to adopt the District Court's reasoning, it did so expressly (and with page citations).[2] The Court never stated that it was adopting the District Court's one recovery ruling on the FF&E fraud claim, nor did it refer to the statute (Section 28(a) of the Exchange Act of 1934, 15 U.S.C. § 78bb(a)) or the case law on which the District Court relied.

Instead, the Court of Appeals specifically responded to two of Petitioners' arguments. One argument was that "the District Court erred in dismissing their FF & E fraud claims because the dismissal prevented them from pursuing judgments against all potential joint and severally liable parties." 45 F.3d at 1063. The court responded: "[P]laintiffs have not provided any evidence of bad faith, as is necessary to support a fraud claim." *Id.* at 1064. The court expanded on the point in rejecting Petitioners'

---

[2] For example, in affirming the dismissal of the "Ritz-Carlton" fraud claim, Judge Kennedy wrote: "we affirm the District Court on that issue for the reasons stated in its opinion. *Becherer*, 799 F. Supp. at 781-84." *Id.* at 1065. Similarly, in affirming the dismissal of the claims against the lender, Judge Kennedy wrote: "we affirm the District Court for the reasons stated in its opinion. *Becherer*, 799 F. Supp. at 772-75." *Id.* at 1068.

claim that Merrill Lynch breached its duties as an interim escrow agent by not disclosing SSG's intention to lease:

> [W]e have reviewed the District Court's opinions in this case and find no discussion of when Merrill Lynch learned of SSG's intention to lease the disputed FF & E and whether Merrill Lynch thought that intention contravened the contract. Nor have the Becherer plaintiffs [Petitioners] pointed to any part of the record to show they raised this argument below. We will not address it for the first time on appeal. *Merrill Lynch points to evidence that it reduced its commission [from SSG] so that the project could be completed as promised and that it believed that, with these concessions, SSG could fulfill its end of the contract.*
>
> We earlier addressed the Becherer plaintiffs' allegations regarding Merrill Lynch's projections and SSG's decision to lease FF & E. We will not repeat that discussion here, *except to say the claim has no merit.*

Id. at 1066 (emphasis added).

Petitioners' second argument was that Petitioners' tort damages would have been different than their contract damages and, therefore, they should be able to recover on both claims. The Court of Appeals disagreed, finding that under these circumstances, the District Court's measure of contract damages – the full amount of the lease payments, plus interest – "make plaintiffs whole. Plaintiffs, therefore, are not entitled *to recover* under any tort theory, as that would result in a windfall to plaintiffs." *Id.* at 1064 (emphasis added). The Court of Appeals held that Petitioners could not *recover* in *both* tort and contract where the measure of damages is the same,

not that Petitioners could not seek judgments under both theories.

REASONS FOR DENYING THE WRIT

I. THE PETITION SHOULD BE DENIED BECAUSE THE COURT OF APPEALS DID NOT MAKE THE RULING ON WHICH PLAINTIFFS SEEK REVIEW.

The "Questions Presented" in the Petition relate solely to the Court of Appeals' alleged interpretation of Section 28(a) of the Securities Exchange Act of 1934, 15 U.S.C. § 78bb, which addresses recoveries under the Exchange Act and provides that a plaintiff may not recover more than actual damages. Question 1 claims that the Court of Appeals misinterpreted the statute. Question 2 claims that the Court of Appeals' misinterpretation denied Petitioners due process. The body of the Petition confirms its limited scope. (Petition, pp. 2, 11).

The Petition mistakenly challenges the earlier ruling of the *District Court*, which cited Section 28(a). The Court of Appeals did not interpret, cite or rely on Section 28(a) because the statute was not part of its decision. Rather, the Court of Appeals relied upon an alternate ground to affirm the District Court – the lack of evidence of fraud. Thus, the Petition is misdirected to a ruling the Court of Appeals never made.

II. THE PETITION SHOULD BE DENIED BECAUSE PETITIONERS DO NOT SEEK REVIEW OF THE COURT OF APPEALS' HOLDING THAT PETITIONERS FAILED TO PRODUCE EVIDENCE OF FRAUD BY MERRILL LYNCH, WHICH IS AN INDEPENDENT GROUND FOR AFFIRMANCE.

The Court of Appeals affirmatively ruled that "[P]laintiffs have not provided any evidence of bad faith, as is necessary to support a fraud claim." *Id.*, at 1064. Petitioners waived any challenge to that holding when they failed to include it in their Questions Presented. Sup. Ct. R. 14.1; *Izumi Seimitsu Kogyo Kabushiki Kaisha v. U.S. Philips Corp.*, ___ U.S. ___, 114 S.Ct. 425 (1993).

Petitioners' failure to include the Court of Appeals' bad faith ruling in their Questions Presented is fatal to their Petition. Petitioners do not dispute that scienter is an essential element of their fraud claims. *See, e.g., Ernst & Ernst v. Hochfelder,* 425 U.S. 185 (1976) (claim under Section 10(b) of Securities Exchange Act of 1934, 15 U.S.C. § 78j(b)). In support of its summary judgment motion, Merrill Lynch offered unrebutted deposition testimony and documents proving that prior to closing, Merrill Lynch reduced and restructured its fees, eliminating, it believed, any need to lease the FF&E. The Court of Appeals, relying on that unrebutted evidence, correctly held that Petitioners failed to offer evidence demonstrating either intentional fraud or recklessness by Merrill Lynch. Thus, whether or not the Court of Appeals adopted the District Court's one recovery ruling, the Court of Appeals' ruling on the lack of fraud is an independent basis for affirmance not challenged by the Petition. The Petition should therefore be denied.

III. THE COURT OF APPEALS' HOLDING THAT PETITIONERS FAILED TO PRODUCE EVIDENCE OF FRAUD BY MERRILL LYNCH IS NOT APPROPRIATE FOR REVIEW BY THIS COURT.

Even had Petitioners challenged the ruling on the lack of evidence of fraud, the Petition should still be denied. The Petition would be nothing more than a challenge to summary judgment in what the Court of Appeals aptly characterized as "complicated commercial litigation". 43 F.3d at 1057. Having held that Petitioners failed to adduce evidence of fraud, the Court of Appeals correctly concluded that Merrill Lynch was not liable for fraud. This Court will not grant certiorari to review evidence or inferences drawn from it. *General Talking Pictures Corp. v. Western Electric Co.*, 304 U.S. 175 (1938).

Petitioners cite no case holding that granting summary judgment on fraud claims for failure to adduce evidence of scienter is improper. Thus, the Court of Appeals' decision is consistent with decisions of this Court and other Courts of Appeals.

Nothing in the Court of Appeals' decision represents a departure from the accepted and usual course of judicial proceedings. Contrary to Petitioners' assertion, the Court of Appeals did not, by holding Petitioners could not prove an essential element of their claim, impermissibly "make initial findings of fact." (Petition, p.10, n.3).[3]

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[3] *Tidelands Royalty B. Corp. v. Gulf Oil Corp.*, 804 F.2d 1344 (5th Cir. 1986) and *Miller v. Hedlund*, 813 F.2d 1344 (9th Cir. 1987), cited by Petitioners, offer them no support. In *Tidelands*, the Court of Appeals remanded the case to allow Tidelands to

Summary judgment does not involve findings of fact. Rather, it involves a legal ruling as to the *absence* of material issues of fact.

It was, moreover, proper for the Court of Appeals to affirm the dismissal of the FF&E fraud claim based on grounds advanced in, but not relied upon by, the District Court:

> Even though summary judgment was granted on [one ground] . . . , we can affirm the district court on the alternate grounds asserted below. . . . *A grant of summary judgment may be affirmed on a legal basis not ruled upon below.* We may affirm even in situations where the district court's ruling was incorrect, as long as the result was proper.

Missouri Pacific R. Co. v. Harbison-Fischer Mfg. Co., 26 F.3d 531, 538 (5th Cir. 1994) (citations and internal quotations omitted). The Court of Appeals relied on a ground properly before it. In the District Court, Merrill Lynch had briefed and argued for summary judgment on the FF&E claim because there was no evidence of scienter. Merrill Lynch renewed its motion after the SSG contract trial and

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amend its pleadings to assert a new claim. The court understandably declined to determine whether Gulf would be entitled to summary judgment on an unpleaded claim. *Miller* held that the district court erred in granting defendants summary judgment based on immunity and remanded the case for further proceedings on the merits, because resolution of the case depended on unresolved factual issues. Neither case suggests that the Court of Appeals could not grant summary judgment on a ground raised in, but not relied on by, the District Court if the record demonstrated the absence of a material issue of fact.

argued this ground in the Court of Appeals. The Court of Appeals considered a fully developed record.

Petitioners assert that they offered evidence of Merrill Lynch's "uncontroverted knowledge that SSG intended to lease substantial FF&E to finance construction cost overruns . . . " (Petition at 6). However, as the Court of Appeals recognized, Petitioners never rebutted the fact that Merrill Lynch reduced and restructured its fees in order to eliminate the need for leasing. Not only did Merrill Lynch (and SSG) controvert Petitioners' assertion, but Petitioners completely failed to offer evidence that Merrill Lynch knew that SSG would lease the FF&E in the future and that Merrill Lynch intentionally concealed that information from Petitioners.

Moreover, some of the evidence alluded to by Petitioners was not considered by the District Court because they filed it late. The Court of Appeals affirmed the rejection of the untimely materials:

> The affidavits relied upon by the Becherer plaintiffs, both below and on appeal, were not filed with the District Court until the morning of the scheduled hearing on their motions. . . . The Becherer plaintiffs have not provided any

explanation for the tardy filing.[7] Thus, the District Court did not abuse its discretion in refusing to consider the affidavits.

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[7] We also note that the Becherer plaintiffs did not even allege that the District Court erred in refusing to admit these affidavits until their reply brief. Ordinarily, we will not consider assignments of error raised so late in the appeal process.

Id. at 1065-1066. Thus, the Court of Appeals' ruling on the lack of evidence of fraud should not be reviewed.

Finally, Petitioners attempt to bootstrap the granting of summary judgment into a due process violation. Petitioners incorrectly assert that the dismissal of the FF&E fraud claim under Section 28(a) was a denial of substantive due process because the District Court found that the claim had factual and legal merit when it initially denied Merrill Lynch's motion without prejudice. (Petition at 17). However, the Court of Appeals never discussed Section 28(a), and the District Court never held that the FF&E fraud claim had factual and legal merit. The District Court denied Merrill Lynch's initial summary judgment motion *"without prejudice"* because there "may" be questions of fact. This denial of summary judgment was not a finding that Petitioners had offered sufficient evidence in support of their claims. *Forest Hills Early Learning Center, Inc. v. Lukhard*, 728 F.2d 230, 245 (4th Cir. 1984) ("Even when summary judgment is appropriate on the record so far made in a case, a court may properly decline, for a variety of reasons, to grant it. *See generally*, 10A C. Wright, A. Miller and M. Kane, Fed. Practice & Procedure: Civil § 2728 (1983).")

Petitioners' disagreement with an adverse court ruling does not create a substantive due process issue. "[N]o one would claim (or at least no one has yet claimed) that a substantively correct determination of sufficiency of evidence . . . is a federal constitutional right." *TXO Production v. Alliance Resources Corp.*, ___ U.S. ___, 133 S.Ct. 2711, 2727 (1993) (Scalia, J., concurring). Petitioners claim they had meritorious claims; the Court of Appeals disagreed. Petitioners believe the Court of Appeals erred, as does every other petitioner to this Court. Petitioners cannot transform this case into one worthy of review by repackaging a claimed error of law as a denial of substantive due process.

CONCLUSION

The Petition should be denied because the Court of Appeals did not make the "one judgment" ruling which is the sole basis of the Petition. Instead, the Court of Appeals relied upon an independent ground for affirmance not challenged by Petitioners. The Court of Appeals' ruling on this alternate ground is also not appropriate for review by this Court.

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Dated: September 6, 1995

No. 95-44

Supreme Court, U.S.
FILED
SEP 13 1995
CLERK

In The

Supreme Court of the United States

October Term, 1995

RICHARD C. BECHERER, et al.,

Cross-Petitioners,

v.

J. DON ADAMS, MERRILL LYNCH, PIERCE, FENNER & SMITH, INCORPORATED, et al.,

Cross-Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Sixth Circuit

BRIEF IN OPPOSITION TO CROSS-PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED

I.

Whether the Petition should be denied because Petitioners do not seek review of the Court of Appeals' holding that Petitioners failed to provide evidence of fraud by any of the Respondents.

II.

Whether the Petition should be denied because the Court of Appeals' holding that Petitioners failed to produce evidence of fraud by any of the Respondents is not appropriate for review by this Court.

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COUNTER-STATEMENT OF THE CASE

I. PRELIMINARY STATEMENT

Respondents Shelter Seagate Corporation ("SSG"), Can-American Corporation, Can-American Realty Corporation, Arni C. Thorsteinson, Garrett G. Carlson, and Graham C. Lount ("SSG Respondents") adopt and incorporate herein the Questions Presented, the Counter-Statement of the Case and the Reasons for Denying the Writ as set forth by Merrill Lynch, Pierce, Fenner & Smith, Inc., Francis Lavin and Martin Cicco ("Merrill Lynch Respondents") in their Brief in Opposition to Cross-Petition for Writ of Certiorari served on September 6, 1995. This brief supplements but does not repeat the facts and arguments set forth in Merrill Lynch's brief.

II. BACKGROUND

The Registry Resort Hotel is an elaborate 474-room structure built on a fifteen-acre site in Pelican Bay, Florida, adjacent to the Gulf of Mexico. The hotel consists of a nineteen-story tower with 474 guest rooms, including a presidential suite, approximately 144,000 square feet of support facilities containing a variety of shops, three restaurants, a cocktail lounge, a health center, a 1,500-seat ballroom with stage and production capabilities, meeting rooms and a swimming pool. To the east of the tower are fourteen one- and two-story buildings containing fifty cabana guest houses, seven tennis courts, a pro shop, and yet another swimming pool. *Condé Nast Traveler Magazine* has regularly named the hotel one of the country's top twenty resort hotels. The hotel cost approximately $90

million to develop, build, and furnish. SSG was the hotel's developer.

Money was raised for the hotel's development and construction by selling interests in the hotel through a private placement exempt from registration under the securities laws pursuant to Regulation D. SSG was the issuer. Merrill Lynch was the exclusive selling agent. The offering closed into escrow on February 15, 1985. On that date, investors were irrevocably bound to pay for the hotel.[1] Construction of the hotel began shortly after the escrow closing. Once construction of the hotel was substantially complete, SSG was obligated to close the sale and transfer ownership of the hotel to investors. The closing of sale occurred on October 31, 1986.

When the hotel's investors determined it was not as profitable as expected and not the tax shelter envisioned, they commenced this class-action suit against nearly everyone that had anything to do with the development, design, construction, and financing of the hotel, alleging a myriad of claims including prolix allegations of fraud. After three years of litigation, including a trial on Petitioners' breach of contract claims, the District Court determined that Petitioners had failed to prove even a prima facia case of fraud against any of the Respondents. The District Court did find that SSG had breached its contract with Petitioners by leasing certain furniture, fixtures, and equipment ("FF&E") for the hotel.

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[1] *Becherer v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 799 F. Supp. 755, 763 (E.D. Mich. 1992).

Petitioners asserted a fraud claim arising out of SSG's leasing of certain FF&E. The District Court dismissed this claim as well as all of Petitioners' other fraud claims. Petitioners assert before this Court that the District Court's dismissal of Petitioners' FF&E fraud claim deprived them of a "valuable property right" because they assert their claim had factual and legal merit. However, the District Court found, and the Court of Appeals affirmed, that Petitioners "have not provided any evidence of bad faith, as is necessary to support a fraud claim." *Becherer v. Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 43 F.3d 1054, 1064 (6th Cir. 1995). Petitioners' failure of proof is not an issue appropriate for review by this Court.

III. FF&E LEASING

SSG leased two categories of FF&E for the hotel: (1) equipment commonly leased in the hotel industry including televisions and telephones; and (2) kitchen and laundry equipment in order to fund additions and improvements to the hotel which SSG believed were beyond its contractual obligation to provide, but which, as hotel agent, it believed was in the long-term best interests of the hotel. It was uncontroverted before the District Court that SSG believed that the contract documents gave it authority to lease both types of equipment. In fact, prior to leasing, SSG obtained opinions from two lawyers who, after reviewing the contract documents, determined that SSG had contract authority to lease.

The private placement memorandum ("PPM") disclosed the fact that SSG would lease a telephone and

television for each unit and would also lease FF&E for the common areas that were normally leased in the hotel industry.

> . . . [T]he AUO on behalf of each investor will lease a telephone and television set for his Hotel Unit from an independent lessor, and the lease payments will be common expenses.

(PPM at 25.)

> Hotel Agent [SSG] is authorized to rent equipment, furniture and furnishings, including, but not limited to, telephone equipment, front desk and office equipment and furniture, and computers, small appliances, interior plants, signage, TV satellite antennae, and billboards on behalf of all investors.

(PPM at 30.)

SSG also believed it had authority to execute a lease to fund additions and improvements to the hotel beyond that it was contractually obligated to provide, if it determined the additions and improvements were prudent.

The Agency Agreement, one of the contract documents executed by each investor, gave SSG specific authority to make necessary additions or improvements to the hotel. The Agency Agreement gave SSG the authority:

> . . . to make or install . . . *at the expense of the Owner, all necessary or desirable* repairs, decorations, renewals, revisions, alterations, rebuildings, replacements, *additions and improvements* in and to the Hotel.

(Agency Agreement, § 2.1(f) at F2, emphasis added) and,

> . . . to enter into leases on behalf of owner . . . with respect to equipment, furniture, furnishings and fixtures in the commercial unit upon such terms, provisions and conditions as hotel agent shall determine in the exercise of its prudent judgment.

(*Id.* at § 2.1(m) at F3.)

After the hotel's final architectural drawings, plans and specifications were in place and approved by the hotel's operator, after the closing into escrow occurred and investors were irrevocably bound to the purchase, and after construction of the hotel had begun, the Ritz Carlton Hotel, which was located near the Registry site, began operations. The hotel's operator urged SSG to add $2.5 million to the hotel's preopening budget and working capital, to build a $225,000 presidential suite, and to add almost $500,000 in other improvements and additions to the hotel's physical structure to enable the Registry to more effectively compete with the Ritz. SSG concluded that the suggestions were prudent. Accordingly, SSG added to the preopening budget and made the other requested additions and improvements to the physical structure. It entered into a $2.8 million lease with Mellon Bank to finance these additions and improvements.[2]

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[2] The evidence before the District Court was uncontroverted that, at the time of the escrow closing, SSG and Merrill Lynch believed that leasing would not be necessary. The Court of Appeals recognized that Petitioners never rebutted this proof. 43 F.3d at 1066.

The District Court found that SSG's FF&E leasing breached its contract with Petitioners. The District Court dismissed Petitioners' FF&E fraud claim, holding that Petitioners had been made whole by a $6.7 million damage award which included all of the lease payments, lost tax credits, and interest. 799 F. Supp. at 777. In deciding the measure of damages, the District Court found that there was no evidence of malicious, deliberate, willful or wanton fraud. *Id.* at 769. The District Court also found that "plaintiffs have not shown that defendants acted in bad faith, merely that they breached their contract." *Id.* at 776. The evidence before the District Court established that all leasing was done under the good faith belief that it was authorized by the contract.

IV. THE COURT OF APPEALS' HOLDINGS

The Court of Appeals made two holdings with respect to Petitioners' FF&E fraud claim against SSG and the other Respondents. The Court of Appeals held:

> The District Court awarded damages to plaintiffs under a breach of contract theory and found that these damages made plaintiffs whole. Plaintiffs, therefore, are not entitled to recover under any tort theory, as that would result in a windfall to plaintiffs. *In addition, plaintiffs have not provided any evidence of bad faith, as is necessary to support a fraud claim.*

43 F.3d at 1064 (emphasis added).

Thus, with respect to SSG, since contract damages and tort damages were the same, the Court of Appeals held there could be no double recovery. With respect to

the other Respondents, and as an additional basis for affirming the District Court as to SSG, the Court of Appeals held there was no evidence of scienter to support a fraud claim.

REASONS FOR DENYING THE WRIT

Petitioners contend that the District Court deprived them of the opportunity to pursue "cognizable"[3] tort claims against solvent Respondents after awarding contract damages against an insolvent corporation and that the Court of Appeals sanctioned this result. First, the Court of Appeals held that, as to SSG, Petitioners could not recover in both tort and contract where the measure of damages is the same, not that Petitioners could not seek judgment under both theories if they established the prima facie elements of their claim. Second, as to the other Respondents, the District Court's findings of fact establish, and the Court of Appeals held, that Petitioners failed to establish an essential element of their FF&E fraud claim – scienter.

The bottom line is that both the District Court and the Court of Appeals expressly found no fraud in this transaction.

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[3] The District Court expressly stated that Petitioners' FF&E fraud claim was not "cognizable."

I. ON THE RECORD BELOW, PETITIONERS FAILED TO ESTABLISH A PRIMA FACIE CASE OF FRAUD AGAINST SSG, ITS OFFICERS OR AFFILIATE CORPORATIONS.

Without intent to defraud, there is no fraud. *Ernst & Ernst v. Hochfelder*, 425 U.S. 185 (1976); *Iden v. Kasden*, 609 So.2d 54 (Fla. Dist. Ct. App. 1992), *review denied*, 620 So.2d 761 (Fla. 1993). The District Court and the Court of Appeals found this critical element of Petitioners' fraud claim missing. The District Court's and the Court of Appeals' opinions are replete with express findings relating to Petitioners' failure of proof.

A. The District Court Found No Fraud.

First, the District Court said, "[e]ven if the FFE fraud claim was cognizable, plaintiff class is not entitled to recision or punitive damages. . . . There is no evidence of malicious, deliberate, gross, or wanton fraud in this case."[4] 799 F. Supp. at 769.

Second, with respect to determining the measure of damages caused by the leasing, the District Court said: " . . . plaintiff class is not entitled to 'benefit of the bargain' damages, in any event. They have not shown that defendants acted in bad faith, merely that they breached their contract." *Id.* at 776.

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[4] The Cross-Petition's Appendix at App. 11 purports to contain the District Court's August 7, 1992, opinion reported at 799 F. Supp. 755, 769 (E.D. Mich. 1992). However, the first full paragraph reported at App. 36 omits the above-quoted language.

B. The Court of Appeals Found No Fraud.

First, in holding that the FF&E fraud claim against all Respondents had been properly dismissed, the Court of Appeals said: "[i]n addition, Petitioners have not provided any evidence of bad faith, as is necessary to support a fraud claim." 43 F.3d at 1064.

Second, the Court of Appeals held that the District Court erred in piercing the corporate veil and holding three of SSG's officers and two of SSG's affiliate corporations secondarily liable for SSG's breach. The Court of Appeals stated:

> [u]nder Florida law, the corporate veil may not be pierced unless it is shown not only that one business entity dominated or was the alter ego of the other, but that the relationship was created or used in order to mislead or defraud creditors.

Id. at 1064. In reversing the District Court, the Court of Appeals held that ***" . . . there is no evidence that SSG, its affiliates, or shareholders misled or defrauded plaintiffs."*** *Id.* at 1065 (emphasis added). Petitioners have not challenged this finding of no fraud nor have they challenged the Court of Appeals' holding exonerating SSG's officers and affiliate corporations.

Third, in discussing Petitioners' claim that Merrill Lynch breached its interim escrow duties, the Court of Appeals again discussed Petitioners' FF&E fraud claim stating:

> . . . we have reviewed the District Court's opinions in this case and find no discussion of when

> Merrill Lynch learned of SSG's intention to lease the disputed FF&E and whether Merrill Lynch thought that intention contravened the contract. Nor have the Becherer plaintiffs pointed to any part of the record to show they raised this argument below. We will not address it for the first time on appeal.
>
> Merrill Lynch points to evidence that it reduced its commission so that the project could be completed as promised and that it believed that, with these concessions, SSG could fulfill its end of the contract.
>
> We earlier addressed the Becherer plaintiffs' allegations regarding Merrill Lynch's projections and SSG's decision to lease FF&E. We will not repeat that discussion here, except to say the claim has no merit.

Id. at 1066.

In summary, the main reason the District Court dismissed the FF&E fraud claim was because Petitioners failed to establish even a prima facie case of fraud. Based on its review of an extensive 27-volume record, the Court of Appeals agreed. The Cross-Petition does not seek review of these findings and, in any event, the findings are not appropriate for review by this Court.

II. THE COURT OF APPEALS' HOLDING THAT, BECAUSE PETITIONERS HAD BEEN AWARDED CONTRACT DAMAGES, PETITIONERS ARE NOT ENTITLED TO RECOVER UNDER ANY TORT THEORY AGAINST SSG IS CONSISTENT WITH BLACK LETTER LAW.

Assuming that Petitioners had been able to establish a prima facie fraud claim against SSG, its officers or

affiliate corporations, Petitioners proved no damages beyond those supporting their breach of contract claim. It is well-settled that once contract damages have been awarded, Petitioners cannot recover damages in tort unless they allege and prove the existence of additional damages attributable *solely* to the tort. *See, e.g., Rosen v. Marlin*, 486 So.2d 623, *review denied*, 494 So.2d 1151 (Fla. Dist. Ct. App. 1986) (holding that where damages sought in tort are identical to damages sought for breach of contract, damages in tort are not recoverable); *Green Mountain Corp. v. Frink*, 604 So.2d 579 (Fla. Dist. Ct. App. 1992) (determining that plaintiff is not entitled to an independent award of damages for both defendant's fraud and breach of contract where damages sought on fraud claim were the same damages supporting the breach of contract claim); *Rolls v. Bliss & Nyitray, Inc.*, 408 So.2d 229 (Fla. Dist. Ct. App. 1981) (holding that plaintiffs failed to prove that they sustained compensatory damages based on fraud that were separate and distinguishable from compensatory damages based on contract and so failed to establish an essential element of their fraud claim – damages).[5] Even after a full bench trial on the

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[5] It is the law of the case that the contract is to be construed according to Florida law. 799 F. Supp. at 765. Application of the double recovery rule by the United States Circuit Courts is consistent with Florida law. *See, e.g., Atkinson v. Anadarko Bank & Trust Co.*, 808 F.2d 438 (5th Cir. 1987) (holding that plaintiffs cannot recover the same damages twice, even though recovery is based on two different theories); *Mercer v. Davis & Berryman Int'l., Inc.*, 834 F.2d 922 (11th Cir. 1987) (reversing fraud damage award because plaintiff had also been awarded contract damages); *Greenwood Ranches, Inc. v. Skie Constr. Co.*, 629 F.2d 518 (8th Cir. 1980) (finding that plaintiff is entitled to only one

nature and extent of their damages, Petitioners failed to show any damages other than those arising from breach of the contract.

The one recovery ruling of the District Court as to SSG is consistent with Florida and federal law. For the reasons stated above and in the Merrill Lynch Respondents' brief, this holding is not appropriate for review.

CONCLUSION

The District Court and the Court of Appeals did not err, much less depart from the accepted and usual course of judicial proceedings, in dismissing Petitioners' FF&E fraud claim. For six years, Petitioners have continually asserted that this is a fraud case. Two courts have held that they failed to establish even a prima facie case of fraud. The dismissal of the FF&E fraud claim involved the standard application of well-settled law and two courts' repeated acknowledgement of Petitioners' failure of proof. This case involves no important question of

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compensatory damage award even if liability is found on multiple theories).

federal law, and Petitioners' application for a writ of certiorari should be denied.

Dated: September 13, 1995

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